

**Before the  
FEDERAL COMMUNICATIONS COMMISSION  
Washington, DC 20554**

In the Matter of	)	
	)	
Federal-State Joint Board on	)	CC Docket No. 96-45
Universal Service	)	
	)	
1998 Biennial Regulatory Review –	)	CC Docket No. 98-171
Streamlined Contributor Reporting	)	
Requirements Associated with	)	
Administration of Telecommunications	)	
Relay Service, North American Numbering	)	
Plan, Local Number Portability, and	)	
Universal Service Support Mechanisms	)	
	)	
Telecommunications Services for	)	CC Docket No. 90-571
Individuals with Hearing and Speech	)	
Disabilities, and the Americans with	)	
Disabilities Act of 1990	)	
	)	
Administration of the North American	)	
Numbering Plan and North American	)	CC Docket No. 92-237
Numbering Plan Cost Recovery	)	NSD File No. L-00-72
Contribution Factor and Fund Size	)	
	)	
Number Resource Optimization	)	CC Docket No. 99-200
	)	
Telephone Number Portability	)	CC Docket No. 95-116
	)	
Truth-in-Billing and Billing Format	)	CC Docket No. 98-170

**REPLY COMMENTS OF THE COALITION FOR  
SUSTAINABLE UNIVERSAL SERVICE (COSUS)**

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## SUMMARY

The comments confirm CoSUS' initial diagnosis: the existing federal universal service funding mechanism is facing a crisis. No commenter produces economic evidence to refute the clear evidence from the Commission's own reports of telecommunications industry revenues that end user interstate and international telecommunications revenues are shrinking. Those commenters who dispute this fact do so by truncating their data analysis in 1999 or early 2000 – which is like denying that a waterfall exists because you can't see it around the next bend in the river. Not only does the universal service “death spiral” exist, it is already in motion, and it is gaining added momentum as the market itself continues to evolve toward “all distance” products that combine interstate and intrastate telecommunications and information services into a single offering.

Some commenters acknowledge this problem but propose only a set of inadequate band-aid solutions. They argue that the current system can be salvaged by repealing the wireless “safe harbors” (which wireless commenters oppose), expanding universal service contributions to include facilities-based information service provider revenues from information services (which is itself not simple), and moving the existing revenue-based assessments to a “collect and remit” basis rather than lagged reported revenues. While some of these actions would reduce the unreasonably discriminatory aspects of the current revenue-based mechanism, none will ensure that the universal service assessment mechanism will be sustainable and therefore sufficient. These band-aid proposals do not recognize that, as market offerings of bundled interstate telecommunications, intrastate telecommunications and information services continue to increase, the current revenue-

based assessment mechanism will continue to erode. Moreover, the current revenue-based assessment mechanism would continue to be highly inefficient and impose large deadweight economic losses on society.

In addition to CoSUS members, a diverse group of commenters, including large ILECs such as SBC and BellSouth, rural telephone companies such as those represented by NRTA and OPASTCO, and companies such as Sprint that operate across all market segments recognize that a more fundamental change in the assessment mechanism is necessary to secure the future of universal service funding. All of these commenters support moving to a connection-based assessment mechanism in order to ensure a stable, sustainable and sufficient assessment base.

Where these commenters differ is in the precise contours of the connection-based assessment mechanism. Sprint's mechanism is expressly designed to preserve the current level of contribution from wireless carriers as a whole, even though that level of contribution is based on an out-of-date "interim" safe harbor that itself is blatantly, patently, and unreasonably discriminatory. SBC/BellSouth and NRTA/OPASTCO propose connection-based mechanisms that appear to be designed solely to accomplish the allegedly equitable, but in fact merely aesthetic result that carriers providing only interstate transmission without interstate access be assigned some contribution in the first instance. SBC/BellSouth and NRTA/OPASTCO, however, ignore the fact that their proposals would not be competitively neutral because they would impose multiple assessments when a customer receives a service through more than one access provider or more than one interstate transmission provider, but only a single assessment if that same service were provided by a single access provider or a single interstate transmission

provider. Their proposal also would incur significant and unnecessary transaction costs that ultimately would be paid by consumers in the form of either higher USF recovery fees or higher rates. SBC/BellSouth and NRTA/OPASTCO wholly ignore the lessons of the residential PICC: consumers and the public interest are not well served when the Commission adopts indirect solutions that have the veneer, but not the substance, of fairness and honor costly aesthetics rather than simply biting the bullet and accomplishing a collection in the simplest, most direct and straightforward manner.

The CoSUS proposal best meets the statutory requirements that the assessment mechanism be sufficient, equitable and nondiscriminatory. The CoSUS proposal minimizes the transaction costs of the connection-based mechanism, rather than maximizing those costs as SBC/BellSouth and NRTA/OPASTCO would do. And Section 254(d), Section 2(b) and the Commission's 1997 *Universal Service First Report & Order* do not preclude the Commission from adopting the CoSUS proposal.

Protestations that the CoSUS proposal will harm consumers are also not well founded. No commenter provides economic data to refute CoSUS' demonstration that, under its proposal, residential consumers would pay less in universal service recovery fees than under the current revenue-based mechanism, especially as contribution factors continue to rise. Consumers Union *et al.*'s purported impact analysis ignores the fact that consumers today pay ILEC universal service recovery fees that average \$0.51 per line per month, and that this amount will likely rise over the coming year. In any event, no commenter shows any basis for concern over the fact that some consumers will see very small increases in their universal service recovery fees. Implementation of the CoSUS proposal certainly would not cause "rate shock."

Universal service funding today is in a crisis, but there is a solution. The CoSUS proposal is equitable, nondiscriminatory, sufficient and efficient. It will benefit consumers in the aggregate, and it will benefit the public interest by supporting the Act's universal service goals while imposing the least distortion on the rest of the market. The Commission must move expeditiously to end the current highly discriminatory and insufficient universal service funding mechanism with an end user connection-based assessment mechanism.



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**REPLY COMMENTS OF THE COALITION FOR  
SUSTAINABLE UNIVERSAL SERVICE (CoSUS)**

The Coalition for Sustainable Universal Service (“CoSUS” or the “Coalition”), comprised of the Ad Hoc Telecommunications Users Committee, e-commerce & Telecommunications Users Group, AT&T, Level 3 Communications and WorldCom, hereby replies to the comments filed in response to the Commission’s *Further Notice of Proposed*

*Rulemaking.*<sup>1</sup> These comments confirm that reform of the universal service contribution mechanism cannot and should not be delayed. The current mechanism is unsustainable, insufficient, inequitable and unreasonably discriminatory. Universal service funding has entered a “death spiral” of higher contribution factors and lower end user interstate and international telecommunications revenues. The current mechanism cannot be adequately patched. The only solution is to move to a connection-based assessment mechanism.

Among the various proposed connection-based assessment mechanisms, the CoSUS proposal best meets all statutory requirements and will result in an efficient universal service assessment mechanism. All the other proposals are unreasonably discriminatory, and some are grossly inefficient. These inefficiencies themselves are not competitively neutral, and the added costs will be borne by consumers. By contrast, the CoSUS proposal would reduce average residential consumer universal service recovery fees.

The Commission should move expeditiously to adopt the CoSUS plan.<sup>2</sup> The Commission cannot continue to collect universal service assessments under the current mechanism. A new system is needed.

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<sup>1</sup> *In re Federal-State Joint Board on Universal Service; 1998 Biennial Regulatory Review – Streamlined Contributor Reporting Requirements Associated with Administration of Telecommunications Relay Service, North American Numbering Plan, Local Number Portability, and Universal Service Support Mechanisms; Telecommunications Services for Individuals with Hearing and Speech Disabilities, and the Americans with Disabilities Act of 1990; Administration of the North American Numbering Plan and North American Numbering Plan Cost Recovery Contribution Factor and Fund Size; Number Resource Optimization; Telephone Number Portability; Truth-in-Billing and Billing Format*, Further Notice of Proposed Rulemaking & Report & Order, 17 FCC Rcd 3752 (2002) (“FNPRM”).

<sup>2</sup> Draft versions of the rule revisions needed to implement the CoSUS proposal are appended hereto as Attachment 1.

**I. DIVERSE COMMENTERS AGREE THAT THE CURRENT ASSESSMENT MECHANISM IS UNREASONABLY DISCRIMINATORY, INEQUITABLE AND INSUFFICIENT.**

One thing is clear from the initial comments: with the exception of wireless carriers that have a blatantly, patently and unreasonably discriminatory competitive advantage under the current mechanism, virtually no one supports the existing USF contribution system “as is.”<sup>3</sup> Even parties that don’t support the CoSUS proposal largely agree that the current assessment mechanism is inequitable and discriminatory.<sup>4</sup> Moreover, no commenter actually submits economic evidence to show that end user interstate and international revenues are not declining, and many commenters agree that the fund assessment base should be changed, albeit in different ways. The comments support, and do not refute, CoSUS’ basic points: (1) a declining assessment base, increased funding demands and higher contribution factors will lead to a universal service “death spiral,” making the current mechanism unsustainable and therefore insufficient; (2) the wireless “interim” safe harbors are highly and unreasonably discriminatory

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<sup>3</sup> The sole exception appears to be the General Services Administration, which glibly suggests that the contribution factor should simply be allowed to climb *ad infinitum*, no matter how “painful” the experience for contributors. See GSA *FNPRM* Comments at 4. All references to “*FNPRM* Comments” in these Reply Comments are to comments filed in response to the 2002 *FNPRM* in this proceeding. See 17 FCC Rcd 3752 (2002).

<sup>4</sup> See, e.g., ASCENT *FNPRM* Comments at 2 (“ASCENT supports the Commission’s attempts to modify the present USF support mechanism methodology in order to remove certain inequities ....”); CompTel *FNPRM* Comments at 2 (“[T]he current system is broken because it relies too heavily on interstate wireline voice minutes.”); NRTA/OPASTCO *FNPRM* Comments at 5 n.11 (“[I]n light of the rapidity with which the trends discussed above [declining IXC revenues and migration to wireless and IP networks] and in the *Further Notice* are occurring, OPASTCO has re-evaluated its position and is now supportive of a flat-fee methodology ....”); PaeTec Communications *FNPRM* Comments at 2 (“[T]he process of *collecting* USF contributions is fraught with a bureaucratic complexity that runs counter to principles of economic efficiency and fairness, imposes unreasonable burdens on carriers, creates confusion for end-users and detracts from the worthy purposes of universal service.”); SBC *FNPRM* Comments at 5 (proposing a version of a connection-based assessment mechanism); Sprint

and violate the statute; (3) reporting and assessment lags render the current mechanism highly and unreasonably discriminatory and cause the current mechanism to violate the statute.

**A. End User Interstate and International Telecommunications Revenues Are Declining and Are Not a Sufficient Assessment Base.**

**1. The Universal Service Assessment Base Is in a “Death Spiral”**

As CoSUS outlined in its initial comments, if the existing assessment system is not reformed in the near future, the federal universal service fund faces a death spiral. WorldCom underscored that point in stating:

[C]ontribution factors will continue to increase as the assessable revenue pool decreases, and each increase will further reinforce the incentives of customers to subscribe to packages that bundle services with other products in a way that minimizes the portion attributable to interstate services, thereby further decreasing the assessable pool. Those customers for whom bundled service offerings are not a practical alternative will bear an ever-increasing burden.<sup>5</sup>

It is not just CoSUS and its members that have reached the conclusion that the current assessment mechanism is not sustainable. Sprint agrees that “increased use of Internet e-mail services has reduced the number of interstate calls that are placed with IXC’s; and, as the technology improves, many callers could switch to Voice over Internet (‘VoIP’).”<sup>6</sup> Sprint further observes that “the emergence of ‘all distance’ mobile wireless calling plans encourages customers to place more calls using their mobile wireless phones,”<sup>7</sup> which CoSUS previously

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*FNPRM* Comments at 3 (“The system is in urgent need of reform, and Sprint urges the Commission to act expeditiously.”).

<sup>5</sup> WorldCom *FNPRM* Comments at 3-4.

<sup>6</sup> Sprint *FNPRM* Comments at 2.

<sup>7</sup> *Id.*

demonstrated systemically generates less universal service contribution than a wireline long distance call.<sup>8</sup> Sprint estimates that the assessment base today is approximately 9 percent less than it was eighteen months ago.<sup>9</sup> NRTA and OPASTCO concede that “IXC’s interstate revenues may be declining” and that “this places upward pressure on the contribution factor,” especially because long distance carriers’ “contributions presently account for more than half of universal service funding.”<sup>10</sup> In an apparent acknowledgement of the concerns expressed in the *FNPRM* regarding the “long-term stability and sufficiency of universal service support,” SBC and BellSouth offer their own proposal for a connection-based universal service system.

No commenter appears to deny the obvious reality that the universal service assessment cannot be “sufficient” if it is not sustainable. Section 254 as a whole was enacted to address the problem created by the fact that the “patchwork quilt” of implicit and explicit subsidies that predated that Telecommunications Act of 1996 (the “1996 Act”) could not be sustained as competition was introduced to local telecommunications markets.

## **2. Total USF Support Continues to Increase.**

No party denies that total universal service support is increasing. USF support will increase in July 2002 with the implementation of Interstate Common Line Support, and will continue to rise, absent a decision by the Commission to reduce support levels or to better target existing support. Moreover, no commenter disputes the mathematical reality that as total universal service support grows, contribution factors will grow unless the end user interstate and international telecommunications revenues also increase proportionately. Far from increasing,

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<sup>8</sup> See Declaration of Daniel Kelley & David Nugent (“Kelley/Nugent Declaration”), Attachment 4 to CoSUS *FNPRM* Comments, at ¶¶ 17-18.

<sup>9</sup> Sprint *FNPRM* Comments at 5.

<sup>10</sup> NRTA/OPASTCO *FNPRM* Comments at 4.

however, this assessment base is *decreasing*. This decrease means that contribution factors will be rising even without fund increases (as occurred with the Second Quarter 2002 contribution factor), and they will grow substantially as the fund itself increases.

### **3. End User Interstate and International Revenues are Declining.**

No commenter submits convincing evidence to rebut the Commission's own data, which shows that that total end user interstate and international revenues are declining. Those commenters that deny the existence of a declining end user interstate and international telecommunications revenue base, and hence the insufficiency of the existing assessment mechanism, ignore relevant data.

Nextel, for example, *asserts* in bold print that "Overall IXC Revenue Is Not Eroding," but Nextel is then forced to admit that IXC revenues have, in fact, declined over the past three years.<sup>11</sup> Indeed, Nextel's Exhibit 1, which it cites as showing that IXCs have suffered "at most a slight decline in IXC revenues over the past three years," in fact shows that IXC revenue peaked in either 1999 or 2000. This is consistent with NECA data on switched access minutes of use ("MOU"), showing that ILEC switched access MOU peaked during the first two quarters of 2000, and have been in a steady and unprecedented decline ever since.<sup>12</sup> Far from refuting the decline in IXC revenues, Nextel's data confirm it.

NASUCA extrapolates from 1999 toll revenue data to attempt to prove that total interstate toll revenue is not decreasing.<sup>13</sup> Notably, even NASUCA's extrapolation projects a dramatic slowing in growth of interstate toll revenues in 2000. But the other data available show

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<sup>11</sup> Nextel *FNPRM* Comments at 10-11.

<sup>12</sup> CoSUS *FNPRM* Comments at 22.

<sup>13</sup> NASUCA *FNPRM* Comments at 6.

an actual decrease. According to the FCC's Telecommunications Industry Revenue Reports, toll carrier revenue dropped by \$4 billion from 1999 to 2000, from \$60.5 billion in 1999 to \$56.5 billion in 2000.<sup>14</sup>

Moreover, if there were any doubt as to whether this decline in IXC revenues is a sustained trend, as opposed to a one-time phenomenon, those doubts are erased by recent First Quarter 2002 earnings announcements. Across the board, AT&T, Sprint, and WorldCom wireline long distance revenues are down somewhere between 11 percent (for Sprint Global Markets Division voice service and MCI consumer voice service)<sup>15</sup> and 22 percent (for AT&T consumer voice service)<sup>16</sup> compared against First Quarter 2001 revenues. Five days ago, J.P. Morgan released an investment report based on the First Quarter 2002 numbers, noting that while "wireless revenue growth was a positive contributor" to telecommunications revenues, it is likely that "consumer wireline revenues declined at a similar pace to domestic business revenues [across the whole economy]," which the report estimated to have declined by 4.6 percent.<sup>17</sup> This

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<sup>14</sup> Compare J. Lande, Telecommunications Industry Revenues 1999, Table 8, Industry Analysis Division, Common Carrier Bureau (Sept. 2000), with J. Lande & K. Lynch, Telecommunications Industry Revenues 2000, Table 8, Industry Analysis Division, Common Carrier Bureau (Jan. 2002) ("*Telecommunications Industry Revenues 2000*").

<sup>15</sup> MCI Group Summary Financial Information for the Quarter Ended Mar. 31, 2002 <[http://www1.worldcom.com/global/investor\\_relations/financials/files/financials\\_1Q02.pdf](http://www1.worldcom.com/global/investor_relations/financials/files/financials_1Q02.pdf)>, viewed May 9, 2002; Sprint Corp. Selected Operating Results for the Quarter Ended Mar. 31, 2002 <<http://www.sprint.com/sprint/ir/fn/qe/1q02.pdf>>, viewed May 9, 2002.

<sup>16</sup> AT&T News Release, "AT&T Earns 6 Cents Per Diluted Share from Continuing Operations, Excluding Other Expense/Income," Apr. 24, 2002 <<http://www.att.com/news/item/0,1847,10324,00.html>>, viewed May 9, 2002.

<sup>17</sup> "Wireline Service/Incumbents: Another Look Down the Tunnel," U.S. Equity Research, J.P. Morgan Securities Inc., May 8, 2002, at 4.

total consumer wireline revenue decline – which combines local and toll revenue – was attributed “to significant product substitution at the customer level.”<sup>18</sup>

Nextel then posits that long distance revenue declines reflect Bell entry into long distance. To a certain extent, it is correct that some of the long distance revenues lost by the major long distance carriers have gone to the Bell Companies.<sup>19</sup> But it is preposterous to ignore that long distance revenue is declining because of price decreases, substitution of Nextel and other commercial mobile radio service (“CMRS”) wireless services (and e-mail, instant messaging, and Internet searches) for wireline long distance, as well as bundling-driven “leakage” from the system.<sup>20</sup> Moreover, the CoSUS initial comments documented the decline in end user interstate and international telecommunications revenues through far more than the conclusory, “apocalyptic” statements that Nextel decries.<sup>21</sup>

VoiceStream and NASUCA rely on an incomplete data series to support the assertion that interstate switched access minutes continue to climb.<sup>22</sup> The data cited by VoiceStream and NASUCA are masked by the fact that they used annual, rather than quarterly numbers, and have not updated the quarterly numbers for the latest data filed by NECA. Had VoiceStream and NASUCA done so, and graphed the results by quarter, they would have produced Chart 1 in the

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<sup>18</sup> *Id.* at 5.

<sup>19</sup> Nextel *FNPRM* Comments at 12.

<sup>20</sup> *See Ad Hoc FNPRM* Comments at 5.

<sup>21</sup> Nextel *FNPRM* Comments at 11; *see also* U.S. Cellular *FNPRM* Comments at 5-6 (complaining of a lack of data on declining interstate telecommunications revenues).

<sup>22</sup> VoiceStream *FNPRM* Comments at 9; NASUCA *FNPRM* Comments at 7.



CoSUS comments, and they would have discovered that interstate switched access minutes have declined for six straight quarters.<sup>23</sup>

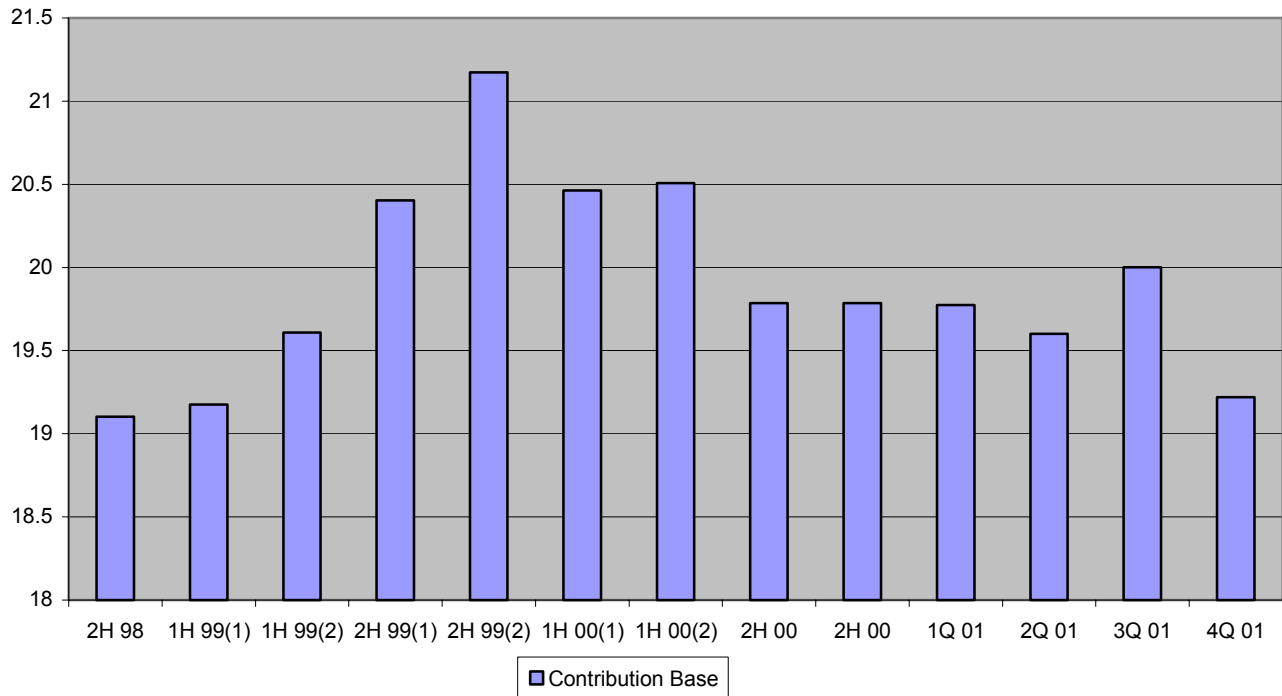
The same problem afflicts VoiceStream's observation that interstate end user telecommunications revenue increased between 1998 and 2001, and NASUCA's assertion that there has been no statistically significant variation in end user interstate and international telecommunications revenues.<sup>24</sup> In fact, when FCC-reported end user interstate and international telecommunications revenues are plotted from the second half of 1999 to the end of 2001, the result, illustrated in Chart A below, shows that end user interstate and international telecommunications revenues peaked in the second half of 1999, and have declined overall since then.

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<sup>23</sup> CoSUS *FNPRM* Comments at 22.

<sup>24</sup> VoiceStream *FNPRM* Comments at 9-10; NASUCA *FNPRM* Comments at 4.

**Chart A**  
**End User Interstate and International**  
**Telecommunications Revenues, 1998 to 2001**<sup>25</sup>



Verizon lamely asserts that it cannot tell “whether any such ‘trend’ [of declining end user interstate and international telecommunications revenues] (if it in fact exists) will continue in the future.”<sup>26</sup> Notably, Verizon does not attempt to support this assertion with an update of its October 2001 economic model. When it filed the results of that model in October 2001, Verizon

<sup>25</sup> The revenue levels are from the FCC’s Universal Service Contribution Public Notices, except for the Second Half 2000 data and the First-Third Quarters 2001 data. The First-Third Quarters 2001 data are from Tables 12-14 of *Telecommunications Industry Revenues 2000*. Half-year data has been divided by two to yield a quarterly average. The second half 2000 data was calculated by subtracting first half 2000 data reported in the FCC’s Universal Service Public Notice for Second Quarter 2001 from the total end user interstate and international telecommunications revenue for 2000 as reported in Table 1 of *Telecommunications Industry Revenues 2000*. NASUCA’s comments listed data by the quarter of the USF Contribution Public Notice, which is not the period for which revenue was actually reported, due to reporting lags. NASUCA also used the quarterly contribution base after adjustment for USAC uncollectibles.

had projected total interstate and international telecommunications revenues would increase slowly each year.<sup>27</sup> However, in the Declaration of Daniel Kelley and David Nugent, CoSUS described several reasons why Verizon's projections were unrealistically optimistic.<sup>28</sup> Verizon's most recent 10-K confirmed the bases for Daniel Kelley and David Nugent's assessment that the Verizon model was overly optimistic: "[Verizon] continues to be affected by competition and technology substitution, as more customers are choosing wireless and Internet services in place of some basic wireline services."<sup>29</sup> Indeed, the Verizon model projected that end user interstate and international telecommunications revenues would be \$1.3 billion higher in 2001 than they actually turned out to be.

The overwhelming weight of the evidence is that end user interstate and international revenues are in fact declining. Unless there is some change made to the universal service assessment mechanisms, these declines will feed the universal service "death spiral" and render the current mechanism wholly insufficient.

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<sup>26</sup> Verizon *FNPRM* Comments at 6.

<sup>27</sup> Letter from W. Scott Randolph, Verizon, to Magalie Roman Salas, Federal Communications Commission, filed Oct. 26, 2001, at 7 ("Verizon Oct. 26, 2001 *Ex Parte*").

<sup>28</sup> Kelley/Nugent Declaration at ¶ 13.

<sup>29</sup> Verizon Communications, Inc. Form 10-K, at 2 (Mar. 20, 2002); *cf.* Kelley/Nugent Declaration at ¶¶ 16-17 ("E-mail and Instant Messaging services, provided over the Internet, have become significant non-telecommunications substitutes for long distance service. ... Wireless service was until recently used primarily for local service. But now wireless companies successfully market regional and national service offerings of low priced buckets of 'all-distance' minutes that include traditional long distance services.").

**4. “All Distance” Packages and Packages of Interstate Telecommunications with Other Services Benefit Consumers But Further Destabilize the Assessment Base.**

BellSouth confirms CoSUS’ observation that bundled offerings are proliferating, stating “the marketplace is witnessing a substitution of bundled local and long distance packages for discrete local and interstate long distance offerings.”<sup>30</sup> BellSouth further acknowledges that bundled wireless and wireline long distance with other service offerings continue to “make it more difficult to identify and segregate interstate revenues.”<sup>31</sup> Contrary to BellSouth’s and Verizon’s assertions, however, the Commission cannot simply prescribe “allocators” to apportion revenue to interstate telecommunications, intrastate telecommunications and non-telecommunications services in an equitable and nondiscriminatory manner. In fact, the experience with the “interim” wireless safe harbors, which were the first “all distance” revenue allocators, suggests that such allocators are not likely to be competitively neutral – and thus are likely to be discriminatory.

BellSouth and Verizon significantly understate the difficulty of the Commission developing what BellSouth calls “a more sophisticated approach to [revenue] identification and attribution.”<sup>32</sup> It is neither administratively reasonable nor technically realistic to attempt to solve the bundling issue by, as Verizon proposes, setting a “default rate” based on an “allocator formula,” or by creating yet another “safe harbor,” all of which could be appealed by carriers “who wanted to be assessed amounts different from those set by the default or safe harbor

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<sup>30</sup> BellSouth *FNPRM* Comments at 3.

<sup>31</sup> *Id.*

<sup>32</sup> *Id.*

formula....”<sup>33</sup> Neither BellSouth nor Verizon offer any details on how such an approach would work. BellSouth instead supports a connection-based plan that avoids problems of revenue identification and attributions. BellSouth’s support for a connection-based alternative speaks louder than its tepid defense of revenue allocation.

As competition increases and the number of end user services no longer subject to regulatory price setting expands – including all CLEC services, all wireless carrier services, all interexchange services, and all ILEC services with pricing flexibility – there is no formula that can be used to determine the appropriate assignment of interstate revenue within a bundled services contract or offering. None of these services set prices according to a separations-based formula. There is therefore no FCC rule that will give the proper interstate revenue allocation for, *e.g.*, the MCI Neighborhood plan, which combines intrastate local service, intrastate toll service, and interstate toll service. Unless the Commission is going to reinstitute tariffs for nondominant carriers and categorically preclude contract arrangements, it cannot possibly derive enough allocators to cover the variation in arrangements and offerings that will exist in the marketplace.

The Commission has often recognized the value of bundled offerings, which encourage consumers to explore new, advanced or specialized services, allow providers to integrate a package of services, and eliminate transaction costs.<sup>34</sup> Ironically, as CoSUS pointed out in its initial comments, if the Commission forced everyone to use one of its two bundling “safe

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<sup>33</sup> Verizon *FNPRM* Comments at 7.

<sup>34</sup> *In re Policy & Rules Concerning the Interstate, Interexchange Marketplace; Implementation of Section 254(g) of the Communications Act of 1934, as Amended; 1998 Biennial Regulatory Review – Review of Customer Premises Equipment & Enhanced Services Unbundling Rules in the Interexchange, Exchange Access, & Local Exchange Markets*, Report & Order, 16 FCC Rcd 7418, 7424-25 (¶ 10) (2001) (“*Bundling Order*”).

harbors,” it would actually discriminate against bundled service offerings in the universal service assessment mechanism.<sup>35</sup> There is no reason for the Commission to continue a regime that distorts and undermines the recognized consumer benefits from bundling, particularly when the CoSUS connection- and capacity-based mechanism would allow the FCC entirely to avoid the need to regulate the amount of revenue to be assigned to various portions of a bundled offering.

Moreover, any allocators created to by the Commission to address bundling of “all distance” services and of telecommunications with non-telecommunications services will likely not be competitively neutral. As discussed further below, the “interim” wireless safe harbors, which were the Commission’s first “all-distance” allocators, have proved to be blatantly discriminatory, and now are unlawful.

With the Commission unable to create an administrable and enforceable set of nondiscriminatory allocators, bundling will continue to destabilize the end user interstate and international telecommunications revenue-based assessment mechanism. This makes moving to a connection-based assessment mechanism imperative in order to sustain universal service and ensure its sufficiency.

**B. The Interim Wireless Safe Harbors Are Unreasonably Discriminatory and Undermine Universal Service.**

The majority of commenters<sup>36</sup> – including some wireless parties<sup>37</sup> – agree with CoSUS that the wireless “interim” safe harbors are unreasonably discriminatory and woefully out of

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<sup>35</sup> CoSUS *FNPRM* Comments at 29.

<sup>36</sup> *See, e.g.*, BellSouth *FNPRM* Comments at 6.

<sup>37</sup> *See* Sprint *FNPRM* Comments at 11 (“For mobile wireless contributors, the contribution should be based on the number of activated telephone handsets, as the Commission suggests.”); U.S. Cellular *FNPRM* Comments at 9 (“USCC would accept elimination of the ‘safe harbor’ percentages which wireless carriers have been able to employ in determining what percentage of their revenues are ‘interstate/international’ in nature.”); Virgin Mobile *FNPRM* Comments at 13

date. The safe harbors – and Sprint’s proposal to perpetuate them<sup>38</sup> – discriminate in favor of wireless carriers at the expense of all other industry segments, thereby conferring a competitive advantage upon wireless carriers over both wireline IXC and wireline LECs.<sup>39</sup> As BT North America put it, “[t]here is no principled basis – including ‘maintaining relative contribution burdens on different industry segments’ – to treat fixed and mobile customers differently.”<sup>40</sup>

Since the “interim” safe harbor percentages were established in 1998, average wireless customer MOU have quadrupled, the number of wireless subscribers has more than doubled, and at least 20 million CMRS customers subscribe to plans that offer nationwide free long distance<sup>41</sup> and that are constantly promoted as offering “free” or “unlimited” long distance.<sup>42</sup> Thus, as NRTA/OPASTCO observe, “it is obvious that the percentage of mobile wireless providers’ total revenue that is attributable to interstate calling is actually much higher than the Commission’s interim safe harbor percentages.”<sup>43</sup> Similarly, even U.S. Cellular (a wireless carrier) concedes that “it may be that in light of the emergence of ‘national’ wireless carriers, with national one rate calling plans, that the percentage of revenues derived from interstate service for those

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(“Virgin Mobile would be willing to give up [the 15 percent “safe harbor”] in return for the administrative simplicity of a connection-based system that allows for real-time pass-through to customers.”).

<sup>38</sup> See Sprint *FNPRM* Comments at 12.

<sup>39</sup> See BellSouth *FNPRM* Comments at 6.

<sup>40</sup> BT North America *FNPRM* Comments at 8 (quoting *FNPRM* ¶ 60).

<sup>41</sup> NTCA *FNPRM* Comments at 6.

<sup>42</sup> See Washington Post, May 5, 2002, at A10 (Cingular ad titled “Never pay long distance or roaming again”); *id.* at A12 (Verizon Wireless ad offering “Unlimited nationwide long distance included”).

<sup>43</sup> NRTA/OPASTCO *FNPRM* Comments at 6; *see also* NECA *FNPRM* Comments at 4 (“[T]he current reporting percentage for CMRS carriers appears to be substantially understated and is long overdue for review and expansion.”).

wireless carriers may exceed the upper safe harbor percentage of fifteen percent.”<sup>44</sup> Moreover, the First Quarter 2002 company-reported revenue numbers detailed above reveal a continuing decline in wireline long distance revenues and rise in wireless revenues.

Even those wireless companies who argue for the preservation of the “interim” safe harbor do not argue that it is competitively neutral as between wireless and wireline long distance providers.<sup>45</sup> As demonstrated in the Declaration of Daniel Kelley and David Nugent, shifting 100 interstate calling minutes from wireline long distance to wireless long distance reduces the amount of universal service contribution collected by 80 percent.<sup>46</sup> The wireless safe harbor is even patently and unreasonably discriminatory as between a wireless connection provider and the ILEC wireline provider. ILEC wireline carriers recover their universal service contributions assessed on their interstate Subscriber Line Charge (SLC) revenues. These recovery charges average \$0.51 per connection per month, irrespective of actual interstate usage. By contrast, cellular, PCS and digital SMR average only \$0.46 per connection per month in USF assessments, including interstate usage subject to the safe harbor.<sup>47</sup> Thus, a wireless carrier, on average, contributes less to universal service than a wireline ILEC, even when the ILEC’s connection is not used to make any interstate calls and the wireless connection is used entirely for interstate usage. This is clear discrimination in favor of one type of provider and one technology over another, and it cannot be justified.

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<sup>44</sup> US Cellular *FNPRM* Comments at 10.

<sup>45</sup> See VoiceStream *FNPRM* Comments at 4-8.

<sup>46</sup> See Kelley/Nugent Declaration at ¶ 18.

<sup>47</sup> *FNPRM*, 17 FCC Rcd at 3777-78 (¶ 59); VoiceStream *FNPRM* Comments at 2; Sprint *FNPRM* Comments at 14. This disparity is all the more remarkable, because the “average” wireless USF assessment actually reflects substantial interstate usage.



VoiceStream's argument that the current mechanism is rational and nondiscriminatory because it reflects the differing interstate revenues reported by each carrier is, with respect to wireless, entirely circular.<sup>48</sup> The only reason wireless carriers' reported interstate revenues are low is because the Commission has adopted a set of "interim" safe harbors that set a cap on reported wireless interstate revenues at 15 percent. With the "safe harbor" set at 15 percent, so long as the total marginal assessment rate on interstate revenues (including interstate universal service) exceeds the total assessment rate on intrastate revenues (including intrastate universal service, if any), a wireless carrier will never report more than 15 percent of its revenues as interstate. In addition, under the current "interim" safe harbor, when a cellular, PCS or digital SMR provider has actual interstate usage of less than 15 percent, it will report less than 15 percent of revenue as interstate, so the safe harbor acts as a cap on reported CMRS interstate revenues.

The inequitable and discriminatory "interim" wireless "safe harbor" cannot lawfully be continued.<sup>49</sup> Although some argue that the solution is simply to update the safe harbors, as discussed in Section II.C below, there is no reason to believe that the Commission can feasibly devise a nondiscriminatory safe harbor.

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<sup>48</sup> VoiceStream *FNPRM* Comments at 4.

<sup>49</sup> Even more absurd is the argument that the wireless safe harbor should be expanded because in the wireline network, interstate dial equipment minutes (DEMS) have declined as a percentage of overall DEMS. VoiceStream *FNPRM* Comments at 7. This argument ignores the impact of dial-up Internet access minutes, all of which are classified as intrastate and the vast majority of which are placed over wireline facilities and not wireless facilities. This argument also ignores wireless substitution for wireline interstate voice traffic, which reduces the overall number of wireline interstate DEMS and skews interstate usage toward wireless.

**C. Reporting Lags Render the Current Mechanism Unreasonably Discriminatory.**

The vast majority of commenting parties agree with the Coalition’s concern that the lag between reported revenues and actual USF assessments means that “[i]t is becoming more and more difficult for IXC’s with decreasing revenues to recover the costs of their payments into the system.”<sup>50</sup> The lag time “is patently unfair to companies with declining revenues that are assessed universal service contributions based upon their higher historical revenues, whereas companies with rising revenues are assessed universal service fees based upon their lower historical revenues.”<sup>51</sup>

It is, therefore, abundantly clear that the Commission should adopt “collect and remit” as a significant reform to the USF contribution mechanism. As AT&T Wireless noted,

Unless the Commission directly addresses the inextricable connection between cost recovery and universal service contributions by moving to a collect and remit system, carriers will continue to face the uncertainties of rising or falling revenues/customer bases and uncollectibles, and line items on consumer bills will continue to fluctuate. As they do today, even with a connection-based system, carriers would have to “back into” a recovery factor months after the Commission tells them how much they owe, taking into consideration over or under-collections from the previous month.<sup>52</sup>

And as other commenters point out, “collect and remit” has been implemented successfully for USF by an increasing number of states, including California,<sup>53</sup> Nevada, Texas, Kansas, Nebraska, Wyoming, and Oregon,<sup>54</sup> and many states use it to collect other fees and taxes.

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<sup>50</sup> Sprint *FNPRM* Comments at 5; *see also, e.g.*, Verizon *FNPRM* Comments at 4-5.

<sup>51</sup> Western Wireless *FNPRM* Comments at 3; *see also* ASCENT *FNPRM* Comments at 18-20.

<sup>52</sup> AT&T Wireless *FNPRM* Comments at 6-7.

<sup>53</sup> *See* California Public Utilities Commission *FNPRM* Comments at 9.

## II. PROPOSED “FIXES” TO THE END USER INTERSTATE AND INTERNATIONAL REVENUE-BASED ASSESSMENT MECHANISM WILL NOT CURE THE PROBLEMS.

### A. “Collect and Remit” or Contributions Based on Projected Revenues Will Not End the “Death Spiral” or Be Adaptable to New Marketing Practices and New Technologies.

As noted above, “collect and remit” is an absolutely essential part of the needed reforms. At the same time, “collect and remit” is not an all-encompassing panacea that will correct all that is woefully wrong with the current USF contribution system. “Collect and remit” will not stop the universal service “death spiral” of increasing contribution factors leading to increased “leakage” through bundled packages in turn leading to even higher contribution factors.

Switching to a “projected cost” basis<sup>55</sup> would likewise not address the basic “death spiral” problem. Even leaving aside the difficulty in accurately forecasting annual USF costs and interstate and international telecommunications revenues across all industry segments, the real problem with the federal USF funding mechanism is not that it lacks “predictability;”<sup>56</sup> the problem is that the relentless decline in end user interstate and international telecommunications revenues is all *too* predictable. Even parties that *favor* a projected-revenue system admit that it “would not address the existing mechanism’s inability to make regulatory distinctions between interstate-intrastate and telecommunications/non-telecommunications revenues ....”<sup>57</sup>

Thus, although either a “collect and remit” revenue-based system or a projected-revenue system has the potential to reduce the anticompetitive effects of the current system, they do

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<sup>54</sup> Sprint *FNPRM* Comments at 15.

<sup>55</sup> See APCIC *FNPRM* Comments at 11-12.

<sup>56</sup> APCIC *FNPRM* Comments at 11.

<sup>57</sup> Arch Wireless *FNPRM* Comments at 11.

nothing to address the other underlying problems that render the current USF contribution mechanism unsustainable and therefore insufficient.

**B. Proposals to Expand Revenue Assessments to “Facilities-based” ISPs Do Not Cure Bundling Problems.**

A small minority of commenters suggest that the Commission require all information service providers (“ISPs”) to contribute to revenue-based universal service funding.<sup>58</sup> The Commission has recently sought comment as to whether certain types of ISPs should have to contribute to USF. As is reflected in the *Broadband Internet Access Framework NPRM* itself,<sup>59</sup> and in the comments filed in that docket, this proposal raises difficult legal and policy questions. And expanding the revenue base to include some or all ISPs is clearly not a “quick fix,” because it will not address the crux of the “death spiral” problem that results from the difficulty of distinguishing interstate and international telecommunications revenues from other revenues.

**C. Eliminating or Updating the Wireless “Safe Harbors” Will Not Be Sufficient to End the “Death Spiral.”**

As noted above, the wireless “safe harbor” is demonstrably and unreasonably discriminatory and is based on outdated assumptions about the nature of wireless telecommunications revenues. It should, therefore, be eliminated, but CoSUS cautions the Commission not to hope that merely putting wireless carriers on equal footing with wireline carriers will be sufficient to avoid the USF “death spiral.” Eliminating or updating the wireless “safe harbors” will not reduce the anticompetitive effects of reporting lags in the current system.

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<sup>58</sup> See, e.g., U.S. Cellular *FNPRM* Comments at 10-12.

<sup>59</sup> See *In re Appropriate Framework for Broadband Access to the Internet over Wireline Facilities; Universal Service Obligations of Broadband Providers; Computer III Further Remand Proceedings: Bell Operating Company Provision of Enhanced Services; 1998 Biennial Regulatory Review - Review of Computer III and ONA Safeguards and Requirements*, Notice of

Nor will it address the fact that interstate telecommunications revenues are declining and in a “death spiral” because the increasing contribution factors creates incentives for carriers and customers to structure contracts to assign revenue to services other than interstate telecommunications. Indeed, the wireless “safe harbors” – and their failure – demonstrate the difficulty of developing nondiscriminatory allocators to halt the “death spiral.”

**D. Proposals to Cap Total Universal Service Support Fail to Address Reality.**

The Coalition is sympathetic to the sentiment that the universal service fund is spiraling upward at a remarkable rate, and agrees with those commenters who think that the expansion is a “proper focus” of the Commission.<sup>60</sup> On the other hand, the expansion is the result of policy choices by the Commission, and at least some of the expansion reflects the FCC’s implementation of the Act’s policies to end implicit subsidies.

The Coalition nevertheless agrees that there should be on-going review of where and how USF money is being spent, and all reasonable efforts should be made to control the size of the fund. At the same time, arguments over the appropriate size of the fund do nothing to address the growing competitive inequities in the assessment mechanism. If the universal service fund were held constant, or even shrank slightly over the years to come, the inequities and discriminations in the revenue-based collection methodology would continue to exist and worsen.

Thus, while the Commission should take steps to wring out excessive subsidies, such actions are not a substitute for also reforming universal service assessments to be equitable,

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Proposed Rulemaking, 17 FCC Rcd 3019, 3053-54 (¶ 78) (2002) (“*Wireline Broadband Internet Access Framework NPRM*”).

<sup>60</sup> See, e.g., Nextel *FNPRM* Comments at 10, 16-17, 29-31.

nondiscriminatory and sufficient. The only alternative to comply with these statutory requirements is to adopt a connection-based assessment mechanism.

### **III. THE COSUS PROPOSAL IS THE MOST EFFICIENT CONNECTION-BASED SOLUTION, AND IT BEST MEETS THE “EQUITABLE AND NONDISCRIMINATORY” REQUIREMENT.**

Although Sprint, BellSouth/SBC and NRTA/OPASTCO propose alternative connection-based universal service assessment mechanisms, all of these alternatives to the CoSUS proposal are not nearly as competitively neutral, and therefore cannot meet the statutory requirement that assessments be made on an “equitable and nondiscriminatory basis.” In addition, the SBC/BellSouth and NRTA/OPASTCO proposals are inefficient, and impose unnecessary deadweight loss on consumers. Home *et al.*’s proposal to assess contributions for high cost support based on network connections in a nationwide pool is similar to the CoSUS proposal; however, to the extent the Home proposal relies upon a revenue-based mechanism for a portion of universal service assessment,<sup>61</sup> it is subject to the same problems of discrimination and insufficiency that plague the current revenue-based assessment mechanism.

By contrast, no party has shown that the CoSUS proposal is unreasonably discriminatory. In fact, it is by far the most efficient, adaptable to new technologies, and equitable. Of the various connection-based assessment proposals parties have put forward, only the CoSUS proposal meets statutory requirements.

#### **A. All Other Connection-Based Proposals Are Unreasonably Discriminatory and Inequitable.**

Section 254(d) sets forth as a basic requirement that all contributions to universal service be made “on an equitable and nondiscriminatory basis.” None of the connection-based

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<sup>61</sup> See Home Telephone *et al.* FNPRM Comments at 3-4.

assessment mechanisms offered as an alternative to the CoSUS proposal can pass this test, because all discriminate significantly and unreasonably and are inequitable.

Although the Commission has not defined “nondiscriminatory” in the context of Section 254(d), given the fundamental objective of the 1996 Act to foster competitive provision of telecommunications services, “nondiscriminatory” must mean, among other things, competitively neutral. The Commission has defined “competitive neutrality” in universal service to mean that “universal service support mechanisms and rules neither unfairly advantage nor disadvantage one provider over another, and neither unfairly favor nor disfavor one technology over another.”<sup>62</sup> In the *Universal Service First Report & Order*, the Commission concluded that although “given the complexities and diversity of the telecommunications marketplace it would be extremely difficult to achieve strict competitive neutrality,” minimizing departures from strict competitive neutrality would ensure “that no entity receives an unfair competitive advantage that may skew the marketplace or inhibit competition by limiting the available quantity of services or restricting the entry of potential service providers.”<sup>63</sup>

**1. The Sprint Proposal Is Not Competitively Neutral, and Is Therefore Unreasonably Discriminatory.**

Sprint’s connection-based assessment proposal is unreasonably discriminatory on its face because it starts from the proposition that the proportion of total universal service assessments paid by wireless carriers (and hence their customers) should never be higher than it is today.<sup>64</sup> Sprint offers no logical justification for this starting point, which is based on a “interim” safe-

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<sup>62</sup> *In re Federal-State Joint Board on Universal Service*, Report & Order, 12 FCC Rcd 8776, 8801 (¶47) (1997) (“*Universal Service First Report & Order*”).

<sup>63</sup> *Id.* at 8801-02 (¶ 48).

<sup>64</sup> Sprint *FNPRM* Comments at 11-12.

harbor that the Commission established in 1998 just as Sprint and other cellular, PCS and digital SMR carriers were beginning to roll out “all-distance” one-rate plans. As Sprint acknowledges, these plans “include large buckets of minutes with ‘free long-distance.’”<sup>65</sup> In defense of using the current level of wireless contribution as a starting point, Sprint states only that “it is difficult to determine to what extent the growth in wireless usage overall equates with growth in wireless interstate calling” and “there is no record evidence that supports a particular percentage of wireless interstate traffic.”<sup>66</sup>

Sprint’s proposal deliberately results in a wireless connection being assessed a different rate than a wireline connection, even when those connections are at least partial substitutes. Sprint previously estimated that its proposal would result in a \$0.46 per connection per month assessment for mobile connections, but \$2.01 for a wireline connection.<sup>67</sup> Even if Sprint were to propose a \$1.00 fee for residential and single line business connections, similar to the CoSUS proposal, the wireless connection assessment rate would still be half the residential wireline assessment rate.

Sprint’s proposal clearly advantages one technology (CMRS) and one provider (mobile) over another (wireline). While substitution of wireless for primary residential wireline phones is still relatively rare, substitution of wireless for an additional residential wireline connection is

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<sup>65</sup> *Id.* at 13.

<sup>66</sup> *Id.* Nextel’s proposal to “freeze” CMRS carrier contributions is even more discriminatory, as total USF support continues to increase. Nextel *FNPRM* Comments at 23. Nextel makes no attempt justify how such a discriminatory “freeze” on the contributions from one set of providers using one technology could even make a pretense of being nondiscriminatory.

<sup>67</sup> *FNPRM*, 17 FCC Rcd at 3778 (¶ 60); Letter from Pete Sywenki, Sprint, to Magalie Roman Salas, Federal Communications Commission, filed Aug. 8, 2001 (“Sprint Aug. 8, 2001 *Ex Parte*”).



more common.<sup>68</sup> By advantaging one of two competing technologies, Sprint's proposal cannot be competitively neutral. Because it is not competitively neutral, Sprint's proposal cannot meet the statutory requirement that contributions be assessed on an "equitable and nondiscriminatory" basis.

## **2. The NRTA/OPASTCO and SBC/BellSouth Proposals Are Not Competitively Neutral and Assess Non-Assessable Entities.**

The SBC/BellSouth and NRTA/OPASTCO proposals also are not competitively neutral. Both SBC/BellSouth and NRTA/OPASTCO propose that each end user connection be assessed, as well as each end user customer relationship with an interstate service "transmission link" provider.<sup>69</sup> SBC/BellSouth further propose that the assessment on either the end user connection provider (called the "Access QSC") or the interstate transmission link provider (called the "Interstate Transport QSC") be based on the capacity of the "connection."<sup>70</sup> It is not apparent, however, whether the capacity of, for example, an interexchange carrier's connection is based upon the capacity of the connection that the access provider provides, or the capacity of some unspecified part of the interexchange carrier's network.

In the first instance, both of these proposals would not be competitively neutral because they would impose multiple assessments when a customer receives a service through more than one access provider or more than one interstate transmission provider, but only a single

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<sup>68</sup> See *In re Implementation of Section 6002(b) of the Omnibus Budget Reconciliation Act of 1993; Annual Report and Analysis of Competitive Market Conditions With Respect To Commercial Mobile Services*, Sixth Report, 16 FCC Rcd 13350, 13381 & n.216 (2001).

<sup>69</sup> NRTA/OPASTCO *FNPRM* Comments at 12; SBC *FNPRM* Comments at 10 (SBC/BellSouth refer to the "Interstate Transport QSC").

<sup>70</sup> SBC and BellSouth do not create separate assessment rates for residential lines. They also propose several additional tiers, although they do not include any explanation of why the additional tiers are needed or the reasons for the proposed assessment levels for those tiers. See SBC *FNPRM* Comments at 10-11.

assessment if that same service were provided by a single access provider or a single interstate transmission provider. If, for example, a business user purchases a channel termination from an ILEC under tariff, but purchases transport from that channel termination to the interexchange carrier's POP from a CLEC, under both the NRTA/OPASTCO and SBC/BellSouth proposals, that business user would incur two USF connection fees. However, if that same user purchased a special access service from the ILEC, it would incur only one USF connection fee. SBC and BellSouth neither acknowledge nor justify this result, which unfairly burdens one configuration of providers offering the same service to the same customer. Similarly, under both proposals, if a user assembles a multistate private line network using one provider from New York to Philadelphia and a second provider from Philadelphia to Washington, DC, that user would incur two USF connection fees, but if it assembled the same network using only a single provider, it would incur a single USF connection fee.<sup>71</sup> This cannot meet the statutory requirement that assessments be "equitable and nondiscriminatory."

In addition, the SBC/BellSouth and NRTA/OPASTCO proposals would likely not be competitively neutral because connections have little relationship to the manner in which interstate long distance services, particularly voice services, are provided. The nature and capacity of the connection between the end user and the ILEC switch is of no relevance to the long distance carrier that is delivered traffic from the ILEC switch.<sup>72</sup> Customer calls originating on ILEC-provided lines are not treated differently as a result of the ILEC line type.<sup>73</sup> Thus,

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<sup>71</sup> AOL-Time Warner warns against adopting a system of surcharges on intermediate transmission links, rather than end user transmission links. *See* AOL Time Warner *FNPRM* Comments at 8.

<sup>72</sup> *See* Declaration of Alan Lentz and Mark Milota ("Lentz/Milota Declaration"), appended hereto as Attachment 2, at ¶ 4.

<sup>73</sup> *Id.*

while access connection providers such as LECs or wireless carriers may be able to track on a near-real-time basis the number of connections, the long distance segment provider will not be able to do so. Instead, the long distance segment provider, to the extent it is not affiliated with the access provider, will be dependent upon the access provider to provide connection information.

Experience with the PICC charges shows that this is not a trivial problem and that the information lags and gaps will be significant. While the LEC-affiliated interstate long distance segment provider will get accurate information from its LEC affiliate, the unaffiliated long distance provider will have to obtain the connection information and verify it.<sup>74</sup> With PICCs, it turned out to be costly not only to implement systems to collect ILEC line-type information, but also to assemble and keep current a database of ILEC line types for the IXC's embedded customer base. As the unaffiliated IXC must bear these costs while the LEC-affiliated IXC can piggyback on its LEC affiliate, the impact of the SBC/BellSouth assessment on interstate transmission providers will not be competitively neutral.

SBC exacerbates this discrimination from data lags through its end user recovery proposal. SBC proposes that all carriers be given a "reasonable incremental percentage for uncollectibles and billing and administrative expenses."<sup>75</sup> Because the Interstate Transport QSCs would be dependent upon LECs for data, and because LECs will likely demand payment for data, and because Interstate Transport QSCs operate in markets with higher uncollectibles than the LECs, SBC's "safe harbor" approach would favor some providers over others, especially favoring those that provide both the access segment and the interstate transport segment.

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<sup>74</sup> *Id.* at ¶¶ 5-6.

<sup>75</sup> SBC *FNPRM* Comments at 13.

These problems are even more apparent with respect to ISPs, which would be assessed for USF contributions under both the SBC/BellSouth and NRTA/OPASTCO proposals. There is no reason for the ISP – particularly a dial-up ISP – to be concerned with the number of LEC connections that an enrolling customer will use to access the ISP, or the capacity of those connections between the end user and the LEC. Yet these proposals would require the ISP to report and pay universal service assessments based on these connections, and the ISP would have to rely on the LEC to provide accurate and timely data and would be subject to reporting lags and the discrimination inherent in such lags.

**B. The SBC/BellSouth and NRTA/OPASTCO Proposals Are Inefficient and Will Result in Increased Consumer Charges.**

Both the SBC/BellSouth and NRTA/OPASTCO proposals for a connection-based assessment mechanism would be highly inefficient, and will result in higher consumer charges than are necessary to fund universal service on a sustainable and sufficient basis. By assessing both the end user connection and the end user's ability to transmit voice or data across state line or national boundaries, these proposals are "split the baby" schemes similar to the Presubscribed Interexchange Carrier Charge adopted in the Commission's *1997 Interstate Access Charge Reform First Report and Order*<sup>76</sup> and then substantially repealed in the *CALLS Order*.<sup>77</sup> The

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<sup>76</sup> *In re Access Charge Reform; Price Cap Performance Review for Local Exchange Carriers; Transport Rate Structure and Pricing End User Common Line Charges*, First Report & Order, 12 FCC Rcd 15982, 15999 (¶ 38) (1997) ("*1997 Interstate Access Charge Reform First Report & Order*").

<sup>77</sup> *In re Access Charge Reform; Price Cap Performance Review for Local Exchange Carriers; Low-Volume Long Distance Users; Federal-State Joint Board on Universal Service*, Sixth Report & Order in CC Docket Nos. 96-262 & 94-1, Report & Order in CC Docket No. 99-249, Eleventh Report & Order in CC Docket No. 96-45, 15 FCC Rcd 12962, 12964 (¶ 2) (2000) ("*CALLS Order*"), *aff'd in part and rev'd in part, on other grounds*, *Texas Office of Public Utility Counsel v. FCC*, 265 F.3d 313 (5<sup>th</sup> Cir. 2001) ("*TOPUC II*"), *cert. denied sub nom. National*

same factors that made the PICC an inefficient mechanism for collecting common line charges, and that led to consumers paying PICC recovery fees that were 40 percent greater than the ILEC PICC charges, will apply to recovery of USF assessment fees under the SBC/BellSouth and NRTA/OPASTCO proposals. There is no obvious public policy reason for incurring these substantial additional transaction costs: the SBC/BellSouth and NRTA/OPASTCO proposals result in substantial deadweight loss.

Assigning a USF assessment fee to the end user connection provider and a second USF assessment fee to the interstate transport segment does not in any way increase the efficiency of a connection-based assessment mechanism or its sustainability. In the simple case of an ordinary residential consumer with a presubscribed long distance service, the main impact of these proposals is that instead of collecting a single universal service assessment for service to this customer, the SBC/BellSouth and NRTA/OPASTCO proposals would collect two assessments, one from the local interstate connection provider and one from the long distance carrier.<sup>78</sup> There is no competitive neutrality reason to assign the assessments in this manner. Whether the local interstate connection provider's assessment is larger, as under the CoSUS proposal, or smaller, as under the SBC/BellSouth or NRTA/OPASTCO proposal, will make no competitive difference in

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*Association of Regulatory Utility Commissioners v. FCC*, 2002 U.S. LEXIS 2361 (Apr. 15, 2002).

<sup>78</sup> Because the SBC/BellSouth and NRTA/OPASTCO proposals do not cap residential and wireless assessments at an initial level of \$1.00, the residential connection assessments to the access and interstate transport providers respectively will not simply be half the CoSUS proposed residential connection assessment.

competition between competing providers of the local interstate connection, all of whom pay the same assessment.<sup>79</sup>

For the local interstate connection provider, the costs of implementing the SBC/BellSouth proposal, NRTA/OPASTCO proposal and the CoSUS proposal are the same. The provider must implement a system to “count” the connections it provides to end users, and the capacity of those connections. The provider must report those connections to the universal service administrator. And it must collect a charge from its own customer to recover the universal service assessment. The size of the connection assessment does not change these costs.

For the interstate transport provider – the long distance provider in this simplified residential service example – under the CoSUS proposal there are no additional administrative costs incurred because assessments are not made on the interstate transmission relationship. However, under the SBC/BellSouth and NRTA/OPASTCO proposals, there are substantial additional transaction costs incurred. First, the interstate transport provider must obtain the information necessary to determine the number and capacity of connections that it serves.<sup>80</sup> Connection providers are the sole source of this information.<sup>81</sup> CoSUS agrees with NECA’s warning of “the administrative burdens associated with resolving the ‘whose line is it’ problem from disputes between IXC’s and LEC’s reporting different presubscribed line counts.”<sup>82</sup> With respect to PICC charges, for example, long distance carriers never were able to develop a system

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<sup>79</sup> As discussed previously, for more complicated network arrangements than the simple residential example posed here, the SBC/BellSouth and NRTA/OPASTCO proposals would have a negative and discriminatory competitive effect as compared with the CoSUS proposal.

<sup>80</sup> See Lentz/Milota Declaration at ¶¶ 5-6.

<sup>81</sup> See *id.* at ¶ 6.

<sup>82</sup> NECA FNPRM Comments at 9.

to track the number of lines, and the types of lines, served within a given account.<sup>83</sup> Lines for which the customer does not designate a presubscribed carrier (no-PIC lines) would have to be segregated from lines that the customer presubscribes, even at the same location. For PICC implementation, ILECs charged long distance companies substantial amounts to receive accurate line count information, and these costs were recurring as periodic full database updates were needed.<sup>84</sup>

Once the interstate transport provider has accurate data on the number and capacity of the end user connections to which it provides service, it must then calculate and render its payment to the universal service administrator. And then it must recover its USF assessment from its customers. This recovery will necessarily reflect the fact that uncollectibles on long distance accounts are typically higher than for local service providers. It may also mean that assessments for multiple connections are averaged across all residential accounts if accurate and auditable data to match connections to accounts is not available (as was the case with the residential PICC). Moreover, for very low or zero-volume users that an IXC would not normally bill on a monthly basis, the long distance provider must either generate a monthly bill – thereby incurring an additional billing expense attributable solely to universal service assessments – or it must wait to bill that customer in a multi-month bill, creating customer confusion and the appearance of high line charges.

It is important to recognize that the PICC experience actually *understates* the extent to which the SBC/BellSouth and NRTA/OPASTCO proposals would be burdensome and unwieldy. PICCs were implemented only by the price-cap LECs – the nation’s largest ILECs with the most

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<sup>83</sup> Lentz/Milota Declaration at ¶ 5.

<sup>84</sup> *Id.* at ¶ 10.

sophisticated billing and information technology capabilities. And still PICCs proved to be highly inefficient and error-prone. The SBC/BellSouth and NRTA/OPASTCO proposals would require over 1300 other, much smaller ILECs to develop the capability to provide line-type data to IXCs electronically each month. That would surely prove to be even more costly and more error-prone than was the case for the price-cap LEC PICCs.

Moreover, the SBC/BellSouth and NRTA/OPASTCO proposals impose these additional transaction costs not just on long distance carriers, but also on ISPs. ISPs would have to go through the exact same steps, regardless of whether they provided dial-up service, service over broadband transmission facilities provided by another provider, or service over their own broadband facilities. With *over half* of American households now subscribing to Internet access, this is substantial additional transactional cost for all ISPs.<sup>85</sup>

As is apparent from simply describing the administrative steps, the SBC/BellSouth and NRTA/OPASTCO proposals require providers – and ultimately customers – to incur and pay for substantial additional administrative costs beyond those necessary to implement the CoSUS proposal. The result for both business and residential customers is predictable – the total universal service recovery fee paid by customers across all their service providers will be much higher under the SBC/BellSouth or the NRTA/OPASTCO proposal. Experience with residential PICCs showed that the transaction costs were substantial and led to an approximately 40 percent increase in recovery fees above provider assessments. Because SBC/BellSouth and NRTA/OPASTCO also extend assessments to ISPs, the additional costs to consumers are likely to be even higher.

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<sup>85</sup> National Telecommunications and Information Administration, *A Nation Online: How Americans Are Expanding Their Use of the Internet*, at 8 (Figure 1-4).



These added transaction costs of the SBC/BellSouth and NRTA/OPASTCO proposals will also add to consumer confusion. As is the case today, consumers will not understand why they are receiving multiple universal service fees for services provided over the same telephone line. Because the transaction costs are likely to vary from provider to provider and from industry segment to industry segment, the varying level of fees, especially for services over the same connection, will also add to consumer confusion. This is an additional and unnecessary public transaction cost of the SBC/BellSouth and NRTA/OPASTCO proposals.

Again, there is no public policy rationale for incurring these added transaction costs. They do not improve the sustainability of the collection mechanism.<sup>86</sup> They are not necessary to ensure competitive neutrality. They are not necessary to improve the efficiency of the assessment mechanism and to increase consumer welfare and reduce deadweight loss. It should be obvious that collecting and recovering universal service assessments at a single point from one provider in the stream of a communication will be much more efficient than collecting and recovering those assessments from multiple points in the communication path. The main purpose for incurring the added transaction costs of the SBC/BellSouth and NRTA/OPASTCO proposal appears to be aesthetic – to appear to be assessing all carriers regardless of the segment of communications being provided. Such costly aesthetics are not in the public interest, and, as discussed further below, are not statutorily required.

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<sup>86</sup> If the Commission desires to include end user Internet access transmission connections, such as cable modems or satellite links, as assessable connections, it can do so under the CoSUS proposal without incurring the added transactions costs that the SBC/BellSouth and NRTA/OPASTCO proposals entail.

### **C. The CoSUS Proposal Is Nondiscriminatory.**

The comments demonstrate that the CoSUS proposal is nondiscriminatory. No commenter, even those opposed to the CoSUS proposal, convincingly articulates a competitive bias in the CoSUS proposal against a particular provider or technology. As long as carriers are allowed to recover all associated costs of the universal service assessment mechanism, the CoSUS proposal will be competitively neutral.

#### **1. No Unreasonable Discrimination between IXCs and Other Carriers.**

Several parties allege that the CoSUS proposal is unreasonably discriminatory because USF assessments will be made on the carrier that provides the end user connection, and the traditional IXCs provide fewer end user connections relative to interstate telecommunications revenues than do other carriers.<sup>87</sup> As discussed further in Section III.E below, these arguments assume that all universal service assessments must be interstate revenue-based, when in fact the Act imposes no such requirement. Moreover, the argument that a connection-based assessment unreasonably discriminates against interstate connections providers lacks any cogent analytical foundation because it ignores the tremendous inefficiencies of attempting to assess interstate operations other than the provision of the end user connections, as discussed above.

No party that alleges that the CoSUS proposal unreasonably discriminates against interstate connections providers actually articulates any competitive effect of this alleged unreasonable discrimination. No party demonstrates that providers of interexchange services that are unaffiliated with connections providers will somehow have a competitive advantage vis-

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<sup>87</sup> See, e.g., Verizon *FNPRM* Comments at 20-22.

à-vis providers of interexchange services that are affiliated with connections providers.<sup>88</sup> To the contrary, CoSUS has demonstrated that its proposal will end the substantial and unreasonable discrimination against wireline long distance providers in the current universal service assessment mechanism.<sup>89</sup>

Moreover, the distinction drawn between providing the interstate connection, and providing other interstate services, is reasonable. All users of interstate telecommunications services will have an interstate end user connection. An assessment at that point cannot be subject to meaningful bypass, and cannot be avoided or minimized by bundling the interstate connection with intrastate services, information services or customer premises equipment. By contrast, the end user interstate and international telecommunications revenue assessment is subject to erosion from bundling. Collecting universal service assessments at a non-bypassable point helps to fulfill the statutory requirement that support be “sufficient,” and therefore is a rational and nondiscriminatory basis for distinguishing between the provision of interstate end user connections and the provisions of other interstate telecommunications links.

In addition, by collecting the assessments only once, and at a single point for each user, administrative costs are minimized. By contrast, as discussed above, the SBC/BellSouth and NRTA/OPASTCO proposals would maximize administrative costs by imposing them on all interstate providers for all services, necessitating multiple collections for service provided to the same end user and even potentially for the same call. These added administrative costs are also

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<sup>88</sup> Nextel erroneously asserts that a proposal such as the CoSUS proposal would allow ILECs and IXCs to “split” a USF assessment that wireless would bear in full. *See* Nextel *FNPRM* Comments at 15. In fact, under the CoSUS proposal, wireline ILEC, IXC and CMRS operators are each assessed on the connections they provide, and neither the IXC nor the CMRS operators are assessed on their interstate, interexchange operations.

<sup>89</sup> *See* CoSUS *FNPRM* Comments at 17-35.

ultimately paid by consumers, so multiplying USF assessments, and hence recovery fees, also reduces consumer welfare. Avoiding these unnecessary administrative costs is a second rational and non-discriminatory reason for distinguishing between end user interstate and international connections and other telecommunications links that may be provided by interstate telecommunications carriers.

Accordingly, the CoSUS proposal does not unreasonably discriminate between IXC's and other providers of interstate telecommunications services.

## **2. No Unreasonable Discrimination between CLECs and ILECs.**

No commenter points to a way in which the CoSUS proposal would systemically discriminate between ILECs and CLECs. An ILEC that provides a residential connection is assessed the same amount as a CLEC providing the same connection to the same location. The assessment does not vary with the type of services provided over the connection, so it does not benefit providers that can bundle local exchange access and other interstate services.

Time Warner, XO and Allegiance argue that a connections-based methodology with differential multiline business and residential charges would not meet the “nondiscriminatory” requirement because carriers that provide service exclusively or predominantly to multiline businesses would pay a higher percentage of revenues to USF.<sup>90</sup> The Fifth Circuit’s decision in *TOPUC I* does not interpret the statute’s “equitable and nondiscriminatory” requirement to mandate – as Time Warner, XO and Allegiance assert – that either all connections bear exactly the same USF assessment rate or that the assessment rate results in the same percentage of revenues being collected from each carrier.<sup>91</sup> In *TOPUC I*, the Court held only that the

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<sup>90</sup> Time Warner Telecom *et al.* FNPRM Comments at 7.

<sup>91</sup> *Id.*

Commission had not provided an adequate justification of its decision to require COMSAT to pay more in universal service assessments than it collected in total interstate revenue.<sup>92</sup>

All providers of interstate connections to multiline businesses will pay the same amount of universal service assessment per connection under the CoSUS plan as all other providers of interstate connections to multiline businesses. The amount does not vary depending on whether the provider serves exclusively multiline businesses or a mix of multiline businesses and residences. Thus, ASCENT's arguments about impacts on carriers that serve primarily small businesses are entirely beside the point.<sup>93</sup> Moreover, to the extent that there is a public policy reason to assess lower charges on residential connections (with the result of lower residential recovery fees), assessing different rates on residential and multiline business connection is reasonable and does not violate nondiscrimination requirements.

The CoSUS proposal would end one unreasonably discriminatory feature of the current system that can favor CLECs, as well as ILECs with pricing flexibility. Today, CLECs and ILECs with pricing flexibility can adjust the amount of revenue assigned to interstate services on a customer-by-customer contract basis. This allows CLECs to reduce the amount of revenue they report as interstate. A connection-based assessment, because it is not subject to self-designation of revenue from a bundle as "interstate," avoids the discrimination inherent in the current self-designation system. The CoSUS proposal will more reliably ensure that the customers of these CLECs are bearing their fair share of the burden of supporting universal service, and that universal service avoidance cannot be used as a competitive advantage.

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<sup>92</sup> *Texas Office of Public Utility Counsel v. FCC*, 183 F.3d 393, 433-35 (5th Cir. 1999) ("TOPUC I").

<sup>93</sup> See ASCENT FNPRM Comments at 10-12.

### **3. No Unreasonable Discrimination between Wireline and Non-Paging CMRS Providers.**

No commenter can demonstrate that the CoSUS proposal would unreasonably discriminate between wireline and CMRS providers. Under the CoSUS proposal, additional residential lines, the wireline lines most subject to CMRS competition and substitution, pay the exact same USF assessment per connection as CMRS lines. Moreover, wireline-based long distance service and CMRS-based long distance services are treated exactly the same. Unlike the current system – in which incremental long distance minutes provided over a CMRS network pay only 20 percent of the USF contribution that an incremental wireline long distance minute pays and in which the CMRS provider pays less on average in contribution than the ILEC providing an ordinary residential line with no interstate usage<sup>94</sup> – the CoSUS proposal would establish a level playing field between wireline and wireless-based long distance and local services. This is even true when comparing wireless “any distance” service packages with wireline “any distance” packages: under the CoSUS proposal, they pay the same amount of universal service contribution per connection.

Verizon Wireless argues that a connection-based proposal would be unreasonably discriminatory because “landline customers would be assessed only \$1 per month regardless of whether they had one landline phone in their houses or five, while the same customers would be charged \$5 per month if they were to substitute each landline phone in their homes with a wireless handset.”<sup>95</sup> This argument equates an extension phone, which is a handset plugged into the same line and is not a second line, with a wireless phone, which is indeed the equivalent of a second line. This is silly and is like claiming that a party line is the same as single-party

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<sup>94</sup> See Kelley/Nugent Declaration at ¶ 18.

telephone service. The extension phone is merely another location in the house that taps into the same, single connection. By contrast, the landline second, third, fourth and fifth lines and the wireless second, third, fourth and fifth handsets, which are treated the same under the CoSUS proposal, all provide a separate and independent ability to place or receive an interstate call, and all can do so simultaneously. There is nothing discriminatory about the CoSUS proposal's treatment of any kind of multiple, independent connections to a public network.

Verizon Wireless then argues that the fact that each wireless handset can connect independently to a public network cannot justify assessing the interstate connection for universal service. Verizon Wireless asserts, out of thin air and with no logical predicate or legal support, that “there is no legal or factual nexus between a carrier’s or a customer’s connections to the PSTN and universal service contribution obligations.” This is simply not so. An independent connection to a public network allows the user to send and receive interstate telecommunications. Universal service is intended, as Home *et al.* point out, to expand the number of subscribers connected to those interconnected public networks.<sup>96</sup> Verizon then argues that “the USF is designed to ensure the ubiquity and affordability of the network, not its ability to perform at a given peak capacity.”<sup>97</sup> At least as currently constructed, this is also not true. USF will support multiple connections, not just the first connection to a given customer location.<sup>98</sup> In any event, both the Commission and the courts have rejected arguments that a service or

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<sup>95</sup> Verizon Wireless *FNPRM* Comments at 6.

<sup>96</sup> Home Telephone *et al.* *FNPRM* Comments at 4-6.

<sup>97</sup> Verizon Wireless *FNPRM* Comments at 6.

<sup>98</sup> *First Universal Service Report & Order*, 12 FCC Rcd at 8829-30 (¶ 96).

connection must be able to receive funding from universal service in order to be required to contribute to the support of universal service.<sup>99</sup>

VoiceStream argues that the CoSUS proposal would unreasonably discriminate against non-paging CMRS providers because “each industry segment has different levels of end user interstate telecommunications usage.”<sup>100</sup> To the extent that VoiceStream is simply recasting its argument that the current system reflects relative interstate revenues, its argument is circular, as discussed above.<sup>101</sup> To the extent that VoiceStream is arguing that the Act requires contribution according to interstate MOU, the Act contains no such requirement.<sup>102</sup> Indeed, the CoSUS connection-based proposal does not discriminate between providers of wireless and wireline connectors.

Nextel’s argument that the CoSUS proposal unreasonably discriminates against non-paging CMRS providers by allowing wireline local and long distance carriers to “split” an assessment that wireless carriers bear in full is simply wrong.<sup>103</sup> The CoSUS proposal would treat the connection providers, whether wireline or wireless, the same and assess a connection charge. Providers of intermediate links for calls, whether those calls are originated over a wireline connection or a wireless connection, would not be assessed because they are not providing the end user connection. This does not discriminate at all between wireline and wireless providers. Moreover, the distinction that Nextel attempts to make is fast disappearing,

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<sup>99</sup> *Id.* at 9188-89 (¶ 805); *TOPUC I*, 183 F.3d at 420.

<sup>100</sup> VoiceStream *FNPRM* Comments at 5.

<sup>101</sup> See Section I.B, *supra*.

<sup>102</sup> VoiceStream notably omits any mention of its actual percentage of interstate usage.

<sup>103</sup> Nextel *FNPRM* Comments at 20.



with the strong trend of both wireline carriers and wireless carriers to provide all-distance service offerings.

TracFone's argument that the CoSUS proposal would harm wireless long distance vis-à-vis wireline long distance<sup>104</sup> is true only to the extent that the CoSUS proposal would remove the artificial and unlawful discrimination in favor of wireless long distance under the current system. TracFone notably omits any numerical analysis in support of its arguments of discrimination and, indeed, under the CoSUS proposal wireline and wireless connections are treated identically, as are wireline and wireline long distance.

With respect to prepaid wireless, the assertion that there is discrimination between prepaid wireless and prepaid providers that do not provide an interstate connection to public networks but that utilize other connections is simply wrong.<sup>105</sup> Prepaid wireless phones provide both the interstate connection and the interstate transmission.<sup>106</sup> A calling card or dial-around provider, by contrast, provides only the interstate transmission, but not the end-user connection.

#### **4. No Unreasonable Discrimination Against or Among Pagers.**

The CoSUS proposal also does not unreasonably discriminate against or among pagers. The Coalition recognized that assessing pagers the same amount as other CMRS connections could distort consumer purchases of paging services as compared with other CMRS offerings. Accordingly, CoSUS proposed that pagers only be assessed \$0.25, as compared with a \$1.00 per month assessment for PCS, cellular and digital SMR.

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<sup>104</sup> TracFone *FNPRM* Comments at 15-16.

<sup>105</sup> *Id.* at 8; Virgin Mobile *FNPRM* Comments at 14.

<sup>106</sup> OnStar's phones, which provide connections to public networks only when the user subscribes to OnStar's prepaid calling service, should logically be treated like other prepaid wireless offerings and not as a subscription wireless connection. *See* OnStar *FNPRM* Comments at 3-4.

Although various paging commenters assert that the proposed \$0.25 assessment would place them at a competitive disadvantage vis-à-vis other CMRS providers that bundle paging with other services, they offer no data or analysis to support their claim.<sup>107</sup> They provide no evidence that there would be meaningful substitution if, for example, an \$8.00 per month paging service added a \$0.25 universal service recovery fee, but the competing \$45 per month wireless service added a \$1.00 universal service recovery fee. Nor do they provide evidence that the \$0.25 fee industrywide for pagers (as opposed to an individual provider trying to increase its rate by \$0.25 without a similar increase by other providers) would result in substantial numbers of subscribers dropping service or changing service providers.

Setting ratios between cellular and paging USF assessments based on relative current reported interstate revenues is entirely artificial.<sup>108</sup> These reported revenues are based on the existing “interim” safe harbors that were never finalized. As such, they would embed the competitive distortions contained in these interim “safe harbors.”

In any event, even using the existing safe harbor, with the universal service contribution factor likely to exceed 8 percent due to increased funding requirements and falling end user interstate and international telecommunications revenues, a \$0.25 assessment rate would merely require two-way pagers to pay approximately the same amount of contribution they are paying under the current revenue mechanism.<sup>109</sup> It would be no change at all to set initial rates for two-way pagers at this level.

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<sup>107</sup> See, e.g., Arch Wireless *FNPRM* Comments at 12.

<sup>108</sup> See, e.g., AAPC *FNPRM* Comments at 10.

<sup>109</sup> Average monthly revenue of \$25 times 12 percent safe harbor times an 8 percent contribution factor is \$0.24.

**5. No Unreasonable Discrimination between Providers of Different Wireline Business Services.**

The proposal for scaling connection-based charges by capacity tier is competitively neutral, and is not unreasonably discriminatory or a “subsidy” for large capacity users, as ASCENT suggests, nor does it inappropriately burden Centrex, as NRTA/OPASTCO suggest.<sup>110</sup> To ensure that Centrex was not harmed competitively vis-à-vis PBX-based service, the Coalition proposed that Centrex be assessed one-ninth of a Tier 1 multiline business fee per connection. This is the same ratio proposed by Verizon in its comments,<sup>111</sup> and this is the same as the existing treatment of Centrex under the rules for existing ILEC USF recovery fees.<sup>112</sup>

Moreover, the CoSUS proposal incorporates into its tiers the 5:1 ratio for ISDN PRI service suggested by Sprint in its differential between Tier 1 and Tier 2, and thus does not disadvantage ISDN PRI services as Sprint suggests.<sup>113</sup> ISDN PRI service has a capacity of 1.544 bps, so it would be a Tier 2 connection under the CoSUS proposal. Indeed, the Coalition based its Tier 2 charge upon the ISDN PRI SLC relationship of 5:1.<sup>114</sup> This is also the same equivalency ratio as currently applies to existing ILEC USF recovery fees for ISDN PRI service.<sup>115</sup>

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<sup>110</sup> NRTA/OPASTCO *FNPRM* Comments at 20.

<sup>111</sup> Verizon *FNPRM* Comments at 16.

<sup>112</sup> 47 C.F.R. § 69.158 (allowing ILECs to use a 1:9 equivalency ratio for USF recovery charges for Centrex lines).

<sup>113</sup> Sprint *FNPRM* Comments at 14-15.

<sup>114</sup> CoSUS *FNPRM* Comments at 66.

<sup>115</sup> 47 U.S.C. § 69.158.

ASCENT argues that assessing universal service contributions according to capacity-based tiers discriminates against smaller customers and subsidizes large users,<sup>116</sup> and ASCENT proposes that universal service assessments should be based on voice-grade equivalents.<sup>117</sup> The CoSUS proposal for assessments based on capacity tiers would not, however, subsidize large users. Instead the capacity tier proposal, which is also incorporated into the SBC/BellSouth proposal,<sup>118</sup> reflects the fact that the market does not price these facilities on a voice-grade equivalent basis.

Some CLECs have also suggested that a per-connection USF mechanism could distort customer purchasing decisions away from analog or DS-0 lines toward DS-1 lines. These CLECs appears to believe that even if they offer DS-1 service as well as analog and DS-0 services, their current analog and DS-0 customers would attribute the higher universal service charges to the carrier and seek DS-1 service from another carrier. These concerns are not founded in market reality. First, customers who currently have analog service are not likely to shift to DS-1 service simply because of a multiline business USF recovery charge of \$3 per line and a DS-1 USF recovery charge of \$15.<sup>119</sup> In addition, shifting to digital service is itself not cost-free; it would require an initial investment in customer premises equipment of at least \$2,000.

The Commission's goal should be to create a universal service assessment mechanism that affects customer purchase decisions to the least extent possible. The level and amount of

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<sup>116</sup> ASCENT *FNPRM* Comments at 10.

<sup>117</sup> See also Home Telephone *et al.* *FNPRM* Comments at 12.

<sup>118</sup> See SBC *FNPRM* Comments at 10-11, 15.

universal service assessments should not be a material factor for a user in determining whether it purchases multiple DS-0's, a DS-1 or a DS-3 connection. To avoid creating a competitive skew against purchases of higher capacity lines, the universal service assessment tiers must reflect, to the greatest possible extent, the price relationships that exist between a DS-0, DS-1 and DS-3 in the absence of universal service assessments.

Determining the appropriate price ratios is, however, not an easy task. In other contexts, the Commission has grappled with the question of where the crossover point lies between DS-0 and DS-1 services, and it generally has reached no resolution. In the absence of a definitive price study, it is reasonable to use an existing relationship between DS-0 services and DS-1 and other equivalent capacity Tier 1 services. The ISDN-PRI SLC and ILEC universal service recovery fee equivalency ratio provides a reasonable basis for drawing the boundary between Tier 1 and Tier 2 services.<sup>120</sup>

The 40:5 (or 8:1) ratio between Tier 3 and Tier 2 charges approximates the crossover point between DS-3 and DS-1 facilities.<sup>121</sup> No party disputes that this approximates the crossover point for these facilities, and SBC/BellSouth in fact incorporates the same proportion into their connection proposal.

As WorldCom pointed out in its initial comments, basing universal service assessments on voice-grade equivalents, as Ascent and Home Telephone *et al.* suggest, would greatly distort customer procurement decisions. There are 672 voice-grade equivalents in a DS-3. If a Tier 1

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<sup>119</sup> To be conservative, these \$3 and \$15 recovery fees are approximately 10 percent higher than the basic assessment fees. CoSUS members have different positions as to whether such a mark-up for administrative costs should be permitted.

<sup>120</sup> See CoSUS FNPRM Comments at 66.

<sup>121</sup> *Id.*

connection carrier assessment was \$2.75, a Tier 3 connection carrier assessment calculated based on voice-grade equivalents would be \$1848 per connection per month. ILEC prices for these facilities, however, range from \$1000 to \$1500.<sup>122</sup> Under ASCENT's proposal, the USF assessment for a DS-3 could dramatically exceed the price of the DS-3 itself, even without consideration of a mark-up. This would be irrational, and clearly would make universal service a significant factor in customer procurement decisions, rather than minimizing the impact of universal service on customer purchases.

Although less dramatic, the same is true of equivalencies between DS-0's and DS-1's. ASCENT would require that each DS-1 receive 24 Tier 1 connection fees. At a \$2.75 per Tier 1 connection carrier assessment, that would be a Tier 2 assessment of \$66 per connection per month. Such a significant difference, when passed on to end users either with or without a mark-up, could induce customers to purchase additional DS-0's when a DS-1 would be a more efficient and cost-effective choice in the absence of universal service assessments.

ASCENT is really just complaining about the market itself. The Commission has never found that carriers are engaging in unreasonable discrimination when they price the underlying facilities based without regard to the number of voice-grade equivalents. It likewise should not be unreasonable discrimination for universal service assessments to mimic those marketplace pricing structures so as to avoid distorting consumer behavior.

SBC and BellSouth, in their connection-based assessment proposal, suggest additional tiers of universal service assessments, such as assessing a connection of greater than 64 Kbps but less than 1.544 Mbps, or that is asymmetric with a capacity of greater than 6 Mbps, an

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<sup>122</sup> WorldCom *NPRM* Comments at 24 (filed June 25, 2001).

assessment fee of two times the assessment rate for an ordinary 64 Kbps voice line.<sup>123</sup> BellSouth and SBC provide no explanation of why they propose these additional tiers, and why they have proposed the particular charges associated with each tier. SBC and BellSouth do not assert that these additional tiers are necessary to ensure competitive neutrality.

**6. No Unreasonable Discrimination Between IP-Based and Non-IP-Based Providers.**

Although many parties argue that the Commission must include ISP-provided facilities within the scope of universal service contributors, there is nothing about the CoSUS proposal that would preclude the Commission from implementing that result, if it decided that it was necessary to do so to preserve universal service in the public interest. Indeed, it would likely be simpler to implement such a rule under a connection-based assessment mechanism than under a revenue-based mechanism, because a revenue-based mechanism requires segregating services into telecommunications and information services, and segregating revenues into those derived from interstate telecommunications and those derived from information services. Indeed, as Level 3 argued in its reply comments filed in response to the *NPRM*,<sup>124</sup> a connection-based assessment mechanism will be much more adaptable to new Voice-over-IP services than an end user interstate and international telecommunications revenue-based assessment mechanism.

The threat to universal service from erosion by IP-based voice services is not yet imminent, but the erosion of the end user interstate and international telecommunications revenues base is imminent, as is the competitive harm that the current assessment mechanism inflicts on wireline long distance carriers. The Commission therefore can and must move forward to implement a connection-based assessment mechanism without deciding the question

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<sup>123</sup> SBC *FNPRM* Comments at 10-11.

of whether connection facilities self-provisioned by information service providers should be included within the mechanism, unless it can resolve that issue forthwith. The courts have not required the Commission to solve all universal service issues simultaneously, and have given the Commission the leeway to address the most pressing issues first, while deferring less pressing issues for future resolution.<sup>125</sup>

In any event, the CoSUS proposal preserves competitive neutrality between different means of providing residential broadband Internet access service by excluding DSL connections from the universal service mechanism, pending the Commission's decision in the *Broadband Internet Access Framework NPRM*.

**7. No Unreasonable Discrimination Between Growing Carriers and Retrenching Carriers.**

The CoSUS proposal also cures the unreasonable discrimination inherent in the current system against carriers that are retrenching. By incorporating a “collect and remit” process, the CoSUS proposal puts carriers that are retrenching on an even footing with carriers that have a growing market share.

There was widespread and diverse support in the comments for a “collect and remit” assessment mechanism, even among commenters that do not support a connection-based proposal.<sup>126</sup>

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<sup>124</sup> See Level 3 *NPRM* Reply Comments at 14-15 (filed July 9, 2001).

<sup>125</sup> See *Southwestern Bell Telephone Co. v. FCC*, 180 F.3d 307 (D.C. Cir. 1999); *TOPUC I*, 183 F.3d 393.

<sup>126</sup> See Arch Wireless *FNPRM* Comments at 10-11; AT&T Wireless *FNPRM* Comments at 6-7; State of California *FNPRM* Comments at 4, 9; Sprint *FNPRM* Comments at 15-17; Verizon *FNPRM* Comments at 5.



**8. The CoSUS Proposal Reasonably Allocates Burdens between Residences and Multiline Businesses.**

BT argues that it is unreasonable to treat residential and wireless connections differently from multiline businesses. BT, however, cites no support for such a broad assertion, especially when the statute requires that the assessment formula be equitable and nondiscriminatory as between carriers.

Verizon argues that the *FNPRM* would unreasonably burden multiline businesses by making multiline businesses bear a continuing residual responsibility for universal service assessments.<sup>127</sup> On this point, Verizon is correct. However, the CoSUS proposal addresses this problem by setting the multiline business assessment rate as a residual only initially, and then spreading the risk and the benefits of changes in universal service contributions across all users.<sup>128</sup>

**D. The CoSUS Proposal Is Economically Efficient.**

No commenter presents any reasoned analysis that the CoSUS proposal is economically inefficient. Indeed, the evidence is that the CoSUS proposal will substantially reduce existing deadweight economic losses without resulting in substantial additional recurring transaction costs.

Nextel argues that a per-connection proposal would be inefficient because demand for second lines and wireless connections is more elastic than demand for primary wireline connections.<sup>129</sup> Nextel, however, forgets to compare the inefficiency of a per-connection mechanism with the current mechanism, as opposed to having no universal service system at all.

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<sup>127</sup> Verizon *FNPRM* Comments at 16-17.

<sup>128</sup> See CoSUS *FNPRM* Comments at 65.

<sup>129</sup> Nextel *FNPRM* Comments at 7.

While it is true that a per-connection assessment mechanism creates market distortion as compared with having no universal service mechanism, universal service exists as a statutory mandate. Thus, the relevant comparison is between a connection-based assessment mechanism and the current revenue-based mechanism.

When the proper comparison is made between a connection-based mechanism and the current mechanism, Nextel's argument falls apart. Nextel submits no evidence to show that demand for wireline second lines and non-paging CMRS connections is more elastic than long distance service. Indeed, given that wireless plans now tout "free long distance," and have off-peak usage allotments that far exceed the wireline long distance usage of all but a very few, extremely high-volume long distance users, it is unlikely that the elasticity of wireless services exceeds the elasticity of long distance services. So long as long distance is more elastic than wireless, it will still be more economically efficient to move away from an assessment mechanism that primarily surcharges highly elastic long distance usage on what amounts to a usage-sensitive basis, and to begin to surcharge less elastic connections on a non-usage sensitive basis. Nextel has the right goal, minimizing market distortions and limitations on consumer choices, but its goals support adoption of the CoSUS proposal, not retention of the current revenue-based mechanism.

No commenter comes close to demonstrating that the CoSUS proposal will incur recurring or transitional transaction costs that offset the 99.95 percent improvement in consumer welfare that Hausman and Shelanski's analysis suggests would result from substitution of a connection-based universal service mechanism for a revenue-based universal service mechanism. No one contests that there will be transitional costs – but no commenter suggests that these costs

exceed the annual, recurring multibillion-dollar improvement in consumer welfare that a connection-based mechanism would deliver.

Likewise, no party suggests that there would be substantial recurring costs to the CoSUS proposal once carriers instituted the information systems necessary to track the number of connections they were providing to end user customers. Verizon's intimation that it does not and cannot track connections distorts reality.<sup>130</sup> The vast majority of connections – wireline residential, single line business and most multiline business – are tracked today and reported as working “loops” for various FCC and state reports.<sup>131</sup> Wireless carriers similarly report the number of activated handsets for required FCC reports.<sup>132</sup>

What will take some development is a means of tracking and reporting special access and private line connections, and some multiline business connections, according to capacity tiers. Even with respect to these connections, however, Verizon overstates its case. Although Verizon's tariffs may refer to both the connection to the end user and the connection to the IXC POP as “channel terminations,” Verizon has had no difficulty determining the number of channel terminations to customer premises when it needed such information for its pricing flexibility petitions.

**E. The CoSUS Proposal Is Not Precluded by Law.**

Those commenters who oppose the CoSUS proposal argue that it is precluded by law. There is no reason to read the Communications Act to so narrowly constrain the Commission's ability to choose the most sustainable, nondiscriminatory and efficient universal service funding

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<sup>130</sup> Verizon *FNPRM* Comments at 17.

<sup>131</sup> See e.g. ARMIS, FCC Form 477.

<sup>132</sup> See FCC Form 477.

mechanism. Congress in Section 254(d) did “not impose any limitation on how universal service will be funded.”<sup>133</sup> It certainly did not require the Commission to base universal service contributions on revenues, nor did it preclude basing universal service assessments on connections.

**1. The CoSUS Proposal Is Not Precluded by the Commission’s 1997 Universal Service Order.**

Some commenters argue that the *FNPRM* is indistinguishable from the per-line assessment proposal that the Commission considered and declined in 1997, and therefore cannot be adopted.<sup>134</sup> These commenters read far too much into the Commission’s 1997 *Universal Service Order*. No principle of administrative law precludes the Commission from reevaluating its universal service assessment mechanisms in the light of more than four years of operational experience and changing market conditions. The Commission is not bound to its 1997 choices forever, but may adopt a new universal service assessment mechanism if it explains a rational basis for doing so.<sup>135</sup>

When the Commission adopted its revenue-based contribution mechanism in 1997, it clearly did not foresee that there would come a time when interstate and international telecommunications revenues would decline. Indeed, in 1997, the Commission asserted that it had authority to assess universal service contributions based on all telecommunications revenues, not just interstate revenues.<sup>136</sup> At that time, before the introduction of Digital One Rate plans,

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<sup>133</sup> *TOPUC I*, 183 F.3d at 447.

<sup>134</sup> See, e.g., Time Warner Telecom *et al.* *FNPRM* Comments at 12-13; Arch Wireless *FNPRM* Comments at 3.

<sup>135</sup> See, e.g., *Motor Vehicle Mfrs. Ass’n v. State Farm Mut. Auto. Ins. Co.*, 463 U.S. 29, 56, 103 S.Ct. 2856, 2873, 77 L.Ed.2d. 443, 466 (1983).

<sup>136</sup> *Universal Service First Report & Order*, 12 FCC Rcd at 8785 (¶ 14).

the Commission did not know that wireless carriers would offer nationwide “all distance” plans that included “free long distance.” It had not yet seen the harmful and discriminatory competitive consequences of the universal service reporting lags. It did not know that its interstate contribution factors and the associated carrier recovery fees would reach levels that would incent carriers and their customers to offer and to seek bundles of interstate and intrastate telecommunications, information services and customer premises equipment within which providers could minimize the assignment of revenue to the interstate telecommunications component.

Over the past four years, we have seen all of these developments come to pass. Thus, while it was a reasonable prediction by the Commission that an end user interstate telecommunications revenue-based contribution mechanism would be equitable, nondiscriminatory and sufficient, we now know that prediction turned out to be wrong. End user interstate and international telecommunications revenues are not a stable and sustainable base for universal service assessments. The unreasonably discriminatory “interim” wireless safe harbors encourage customers to shift long distance calling from wireline to wireless phones by assessing on the wireless call a far lower universal service contribution. Innovative product bundling, a pro-competitive and pro-consumer market development, is itself undermining the assessment base. There is now more than a sufficient basis for the Commission to conclude that end user interstate and international telecommunications revenues are no longer sufficient, nondiscriminatory and equitable. Indeed, that conclusion is compelled by the evidence submitted on the record to date.

Believing that it had a superior alternative, the Commission in 1997 declined to adopt a line-based assessment mechanism. The Joint Board at that time was concerned that line

“equivalency ratios” could get out of date and become discriminatory.<sup>137</sup> While it remains true that there is a possibility that the ratio of relative assessment rates between tiers could become out of date and distort consumer behavior, this theoretical possibility for discrimination pales in comparison with the actual unreasonably discriminatory results of the current revenue-based contribution mechanism. Moreover, a connection-based mechanism will be much more sustainable, and therefore sufficient, than a revenue-based system, and the Commission must also seek to implement the statutory command that the assessment mechanism be “specific, predictable and sufficient.”

The Commission has changed its policy outcomes on other occasions, and been upheld in court, so long as it has a rational basis for the shift in policy. In its *1997 Interstate Access Charge Reform First Report & Order*, the FCC declined to increase the SLC caps and implemented the residential PICC, citing concerns about the impact of SLC increases on universal service.<sup>138</sup> In the *CALLS Order*, the Commission reversed course, eliminating the residential PICCs and increasing the SLC cap.<sup>139</sup> The Fifth Circuit rejected challenges based on the FCC’s change in policy, stating that the “FCC has articulated rational reasons to the degree that it has changed prior policies.” The Court emphasized that its role was “only [to] examine whether ‘prior policies and standards are being deliberately changed’ and ‘not casually ignored.’”<sup>140</sup> The experience of the last four years, and the shrinking end user interstate and international telecommunications revenue base, provide a more than sufficient basis for the

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<sup>137</sup> *Universal Service First Report & Order*, 12 FCC Rcd at 9210 (¶ 852).

<sup>138</sup> *1997 Interstate Access Charge Reform First Report & Order*, 12 FCC Rcd at 15999 (¶ 38).

<sup>139</sup> *CALLS Order*, 15 FCC Rcd at 12964 (¶ 2).

Commission now to conclude that a connection-based assessment mechanism will fulfill statutory objectives better than an end user interstate and international telecommunications revenue-based assessment mechanism.

## **2. Section 2(b) Does Not Preclude Adoption of the CoSUS Proposal.**

A number of commenters assert that an end user interstate and international connection-based assessment mechanism, such as described in the *FNPRM* and in the CoSUS proposal, would violate Section 2(b). As discussed in CoSUS' initial comments, this argument wildly overreads the Fifth Circuit's decision in *TOPUC I* and ignores the D.C. Circuit's decision in *National Association of Regulatory Utility Commissioners v. FCC*,<sup>141</sup> in which the D.C. Circuit upheld the Commission's authority to create and regulate the interstate subscriber line charge, even though that charge would be levied on a subscriber's local monthly bill, irrespective of the subscriber's interstate usage in a particular month.

AT&T Wireless and Verizon Wireless are therefore wrong when they assert that the assessment of a connection that is used for intrastate communications in addition to interstate communications violates Section 2(b). This is precisely the argument that NARUC raised to challenge the creation of the SLC. It has no more merit with respect to a federal universal service assessment on an interstate connection than it did for an end user line charge on an interstate connection.

Commenters arguing that Section 2(b) precludes an interstate end user connection-based assessment also argue that such an assessment is the functional equivalent of assessing intrastate

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<sup>140</sup> *Bush-Quayle '92 Primary Campaign Comm., Inc. v. FEC*, 104 F.3d 448, 453 (D.C. Cir. 1997).

<sup>141</sup> *See NARUC v. FCC*, 737 F.2d 1095, 1113-14 (D.C. Cir. 1984).

revenues.<sup>142</sup> Such an argument would be demonstrably wrong. An assessment on intrastate revenues would vary as intrastate revenues changed. Thus, when the FCC levied the assessment on intrastate revenues struck down in *TOPUC I*, the FCC would have collected more in federal universal service assessments if carriers were able to increase their intrastate toll or intrastate local service rates. The end user interstate and international connection assessment proposed in the *FNPRM* and in the CoSUS proposal does not vary with local rate increases, or as subscriptions of purely intrastate connections increase. The proposed interstate and international end user connection-based assessments will only vary with the number of interstate connections.

Ironically, the parties that seem to be most adamant that Section 2(b) precludes a connection-based assessment mechanism are CMRS licensees.<sup>143</sup> Of course, CMRS is one of the very few categories of telecommunications that are expressly removed from Section 2(b)'s restriction on FCC jurisdiction.<sup>144</sup> The FCC has previously concluded that Section 332 provided a basis for FCC jurisdiction over all LEC-CMRS interconnection arrangements, without limiting that jurisdiction to arrangements solely for the interconnection and termination of traffic that crosses state boundaries.<sup>145</sup> The fact that Section 254(f) separately authorizes states to assess CMRS providers for contributions to intrastate universal service funds does not alter the fact that

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<sup>142</sup> See, e.g., AT&T Wireless *FNPRM* Comments at 3-5.

<sup>143</sup> See, e.g., *id.*

<sup>144</sup> See 47 U.S.C. § 152(b) (expressly removing Section 332, which governs commercial mobile radio services, from Section 2(b)'s jurisdictional limits).

<sup>145</sup> *In re Implementation of the Local Competition Provisions in the Telecommunications Act of 1996*, First Report & Order, 11 FCC Rcd 15499, 16005 (¶ 1023) (1996).



CMRS lies outside the scope of Section 2(b).<sup>146</sup> CMRS carriers therefore have no standing to argue that they should be protected by Section 2(b)'s limitation on FCC jurisdiction.

**3. Section 254(d)'s Requirement that "Every Telecommunications Carrier" Contribute Is Largely a Non-Issue, and In Any Event Must Be Read in the Context of Section 254(d) as a Whole.**

Several parties that oppose the Coalition proposal argue quite vociferously that a connection-based mechanism would "violate the statutory directive that *every* telecommunications carrier be required to contribute to universal service funding."<sup>147</sup> For all their bluster, these parties ignore the fact that virtually all telecommunications carriers will pay universal service assessments under the CoSUS proposal. The "traditional IXCs" are not exempted from the requirement to pay connection-based assessments when they provide end user connections. Under the CoSUS proposal, AT&T, WorldCom and Sprint will all pay substantial connection-based universal service assessments. The fact that the total assessment to these carriers may be smaller under an end user connection-based assessment mechanism does not change that these carriers would be contributing according to the "equitable and nondiscriminatory" formula adopted by the Commission.

In any event, Section 254(d)'s requirements, including the language that "every telecommunications carrier . . . shall contribute," must all be read in context. As discussed in detail in CoSUS' initial comments, the best reading of Section 254(d) is that the Commission must adopt an "equitable and nondiscriminatory" assessment formula that is applicable to "every telecommunications carrier that provides interstate telecommunications services." Each

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<sup>146</sup> See *Cellular Telecommunications Industry Association v. FCC*, 168 F.3d 1332, 1335 (D.C. Cir. 1999) (holding that Section 332 does not preclude a CMRS provider from being assessed for a state universal service fund pursuant to Section 254(f)).

<sup>147</sup> Rural Cellular Association *FNPRM* Comments at 5.

telecommunications carrier is required to contribute according to that formula. However, if the contributions that would be required to be paid by a specific carrier under that formula are so small as to not justify collection, the FCC can exempt that carrier from payment under its authority to exempt *de minimis* contributions. This interpretation gives full meaning to each part of Section 254(d), and does not elevate some parts over others.

Accordingly, the bare fact that some interstate providers would not pay an assessment does not amount to a statutory violation. As Sprint points out, “254(d) does not require (and has never been read to require) all carriers providing interstate services to contribute to federal universal service funds.”<sup>148</sup> Indeed, the current mechanism will not require a carrier that has substantial interstate telecommunications revenues to contribute if that carrier does not provide service to end users. A carrier incurs no universal service contribution burden under today’s mechanism.

Congress nowhere in Section 254(d) required that universal service assessments be made on the basis of revenues. Had Congress wished to specify that all assessments would be on the basis of revenues, it could have done so explicitly. Congress left it to the Commission to determine the equitable, nondiscriminatory and sufficient formula to use to assess universal service contributions.

SBC incorrectly distorts the scope of the *de minimis* exception, asserting that it only allows the Commission exempt “providers with a *de minimis* amount of interstate activities.”<sup>149</sup> But, as Congress explained, the correct measure of whether a carrier qualifies for the *de minimis* exception is whether “the administrative cost of collecting contributions from a carrier or carriers

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<sup>148</sup> Sprint *FNPRM* Comments at 19.

<sup>149</sup> SBC *FNPRM* Comments at 18.

would exceed the contribution that carrier would otherwise have to make under the formula for contributions selected by the Commission.”<sup>150</sup> The real question in determining the applicability of the *de minimis* exemption is the size of the carrier’s contribution under the Commission’s formula, not the “amount of interstate activities.”

Turning back to the statutory language, it is clear that virtually “every” interstate telecommunications carrier will contribute to the fund under a connection-based approach. Certainly, large carriers such as AT&T and WorldCom will contribute. Some “pure IXCs” will not contribute, just as under the current system “pure carriers’ carriers” do not contribute. In a case where two carriers provide interstate service to a customer – such as where one carrier is an ILEC and the other is an IXC – only one will contribute on behalf of the connection to that customer under a connection-based approach. But the statute does not require that every carrier providing interstate telecommunications service to a customer make a contribution to the universal service fund based on its service *to that customer*. And where a carrier provides interstate telecommunications services but few or no connections, it does not make sense as an administrative matter to require that carrier to contribute to the fund considering that the *de minimis* exception authorizes the Commission to excuse that carrier from contributing.

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<sup>150</sup> H.R. Rpt. No. 104-458, at 131, 104<sup>th</sup> Cong., 2d Sess. (1996) (“1996 Act Conf. Report”).

#### 4. The CoSUS Proposal Is Equitable.

Virtually all commenters that oppose the CoSUS proposal assert that it would be “inequitable.”<sup>151</sup> For the most part, they argue that it would be “inequitable” because interexchange carriers would not be required to contribute to universal service, and the largest portion of interstate revenues, revenues from interstate toll service, would not be assessed.

There is no basis for equating the requirement that contribution be “equitable” with a revenue-based assessment mechanism. Congress did not specify the assessment mechanism, but instead gave the Commission the discretion to fashion the assessment mechanism. Had Congress intended to limit the assessment mechanism to an equitable, revenues based mechanism, it could have added the word “revenue” to the requirement that contribution be made on an “equitable and nondiscriminatory basis.”

Neither the statute nor the legislative history nor the courts have provided further guidance as to the meaning of the requirement that contributions be made on an equitable basis. The Fifth Circuit in *TOPUC I* observed that “obviously, the language also refers to the fairness in the allocation of contribution duties,”<sup>152</sup> but, other than finding that imposing a contribution obligation that exceeded a carrier’s total interstate revenues to be inequitable, does not further explicate the statutory requirement.

One thing that “fairness in the allocation of contribution duties” must mean is that the contributions be competitively neutral. It would not be fair to require one carrier to pay more than a competitor when providing an identical service.

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<sup>151</sup> See, e.g., NTCA *FNPRM* Comments at 3; SBC *FNPRM* Comments at 19.

<sup>152</sup> *TOPUC I*, 183 F.3d at 434.

In further interpreting the term “equitable” there is no reason why the Commission should be constrained to examine the equity of the universal service assessment mechanism through the lens of backward-looking industry service categories. Attempting to divide carriers into “interexchange carriers,” “CLECs,” “ILECs” and “CMRS” boxes to evaluate equity among industry segments ignores the fact that companies that were historically interexchange carriers are now providing local service, companies that historically provided local service are now providing long distance service, and CMRS providers offer “all distance” packages combining local and long distance. Indeed, it is precisely because all companies are moving to offer combinations of intrastate and interstate services without regard to historical categories that the current system is being undermined.

The statutory standard that contribution be “equitable” can therefore be interpreted using a forward-looking view of the industry. Under such a forward-looking view, the key in defining an equitable contribution mechanism is that it be competitively neutral. If contribution is competitively neutral, then it will treat all industry participants fairly and equally, because none will be disadvantaged relative to their competitors.

**F. Transitional Contributor Implementation Costs Are Outweighed by the Need to Create a Sustainable Universal Service Assessment Base.**

Time Warner, XO and Allegiance complain that the CoSUS proposal will require them to institute new information systems to keep track of the number of connections that they provide to their customers. CoSUS has acknowledged that the transition will require carriers to undertake some information technology expenditures.<sup>153</sup> But these one-time transitional costs are necessary in order to preserve universal service. Unlike the unnecessary expenditures that the

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<sup>153</sup> See CoSUS *FNPRM* Comments at 58-59.

SBC/BellSouth proposal would require, these transaction costs would be incurred on a one-time basis by the connection provider.

In addition, XO's declaration is unintentionally revealing in that it contemplates an information system that is extremely manual.<sup>154</sup> It is likely that XO needs an automated information system in any event, and some of the costs cited appear to be costs of automating existing operations.

#### **IV. THE COSUS PROPOSAL DOES NOT HARM CONSUMERS, NOR WILL IT CAUSE "RATE SHOCK."**

A number of commenters assert that the CoSUS proposal will harm consumers.<sup>155</sup> For the most part, these commenters offer no quantitative analysis to back up these assertions, and what little "analysis" is offered is wrong on its face. Moreover, it is inappropriate, arbitrary and capricious to judge consumer impact on, for example, a "wireless customer" while ignoring the fact that that same consumer is also likely to be a "local wireline" customer and a "long distance" customer. No commenter who claims that the CoSUS proposal will lead to reduced demand for their service offers any quantitative evidence of demand suppression from the resulting USF recovery fees that carriers would charge.

##### **A. As CoSUS Demonstrated, Its Proposal Reduces Average USF Recovery Fees for Residential Consumers, Including Low Income Consumers.**

Although many commenters assert that the CoSUS proposal would harm consumers, particularly residential consumers, these assertions lack any analytical foundation. Indeed, NASUCA acknowledges that the CoSUS proposal will benefit residential consumers as a whole

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<sup>154</sup> See Time Warner Telecom *et al.* FNPRM Comments, Attachment 1 (Declaration of Steve Ednie), at ¶ 5.

<sup>155</sup> See, e.g., Verizon FNPRM Comments at 20-21.

in their purchases of wireline telecommunications services.<sup>156</sup> Consumers Union *et al.*'s analysis, once it is corrected for omission of the ILEC USF recovery fees, shows that many consumers will see their total USF recovery fees for wireline telecommunications drop.<sup>157</sup> Corrected versions of Consumers Union *et al.*'s chart are attached hereto, first explaining the impact of including the current average ILEC USF recovery charge of \$0.51 per line, and then explaining the impact if that surcharge *alone* increased to \$0.65 per line.

These comments lend further support to the Declaration of Martha Behrend, which found that both consumers as a whole and low income consumers would be better off, on average, under the Coalition's connections and capacity-based assessment mechanism. Ms. Behrend analyzed TNS data and determined that for the primary residential line, the CoSUS proposal would result in an approximately 40 cent per month reduction in total USF fees, on average for both consumers as a whole and for consumers with less than \$15,000 in annual income.<sup>158</sup> When all consumer purchases of telecommunications – including wireless – are considered, the CoSUS proposal still benefits residential consumers.<sup>159</sup> Furthermore, Ms. Behrend's analysis actually

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<sup>156</sup> NASUCA *FNPRM* Comments at 13.

<sup>157</sup> Consumers Union *et al.* *FNPRM* Comments at Attachment 1. For example, at the average LEC USF recovery fee of \$0.51 per month, under Consumers Union *et al.*'s analysis, the "low use" (29 interstate minutes) AT&T One-Rate Plus Plan customer would actually save \$2.37 per year, and the "average use" (58 interstate minutes) AT&T one-rate plan customer would save \$5.17 per year. If the ILEC recovery fee averages \$0.65 per month, Consumers Union's "low use" AT&T One-Rate Plus Plan customer saves \$4.05 per year, and its "average use" customer on the same plan saves \$5.17 per year.

<sup>158</sup> See Declaration of Martha Behrend ("Behrend Declaration"), Attachment 2 to CoSUS *FNPRM* Comments, at ¶ 4(a) (explaining that, on average, households with income of less than \$15,000 per year will pay \$0.40 per month *less* in USF for their primary residential connection under the CoSUS proposal).

<sup>159</sup> See *id.* at ¶ 4.

overstated the charge on residential consumers because it did not reflect the fact that Lifeline consumers would pay no universal service recovery fees under the CoSUS proposal.<sup>160</sup>

TracFone's asserts that the CoSUS proposal would harm low income consumers and cut off those consumers who use prepaid wireless as their only public network connection.<sup>161</sup> This dramatic assertion is not backed up with any economic support. The Commission should be extremely leery of such assertions, especially given the generally high per-minute rates charged by prepaid wireless companies. To take an example, suppose the Commission imposed a connection fee for each month a prepaid card could be used. TracFone's \$17.99 card for 30 minutes valid for 60 days would increase to \$19.99, or an increase of less than 7 cents per minute for an offering that is already priced at 60 cents per minute. There is no reason to assume that this example would affect the low income user's access to a connection where there are no deposits, credit checks or other barriers. The burden should be on TracFone and other prepaid wireless providers to demonstrate that low income consumers' access will be harmed.

Moreover, no commenter that asserts that the CoSUS proposal would be unfair to "low volume" consumers answers Chairman Powell's challenge to articulate why "low volume consumers' constitute some type of protected class."<sup>162</sup> Although Verizon, in a footnote, repeats its assertions that a per-connection assessment methodology would harm low volume long distance consumers, it provides no rationale for why this is an important public policy consideration,<sup>163</sup> especially at the level of a maximum possible increase of 50-60 cents per

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<sup>160</sup> See *id.*

<sup>161</sup> TracFone *FNPRM* Comments at 10-12.

<sup>162</sup> *In re Low-Volume Long Distance Users*, Notice of Inquiry, Separate Statement of Commissioner Michael Powell, 15 FCC Rcd 6298, 6319 (1999).

<sup>163</sup> Verizon *FNPRM* Comments at n.17.



month.<sup>164</sup> Neither NASUCA nor Consumers Union *et al.* provides a public policy rationale for concern about such a small impact on a small minority of consumers.

Wireless carriers complain that their customers would be “hit with more than a 100% assessment increase.”<sup>165</sup> This, of course, ignores the fact that the vast majority of consumers are not just “wireless” consumers, but they are also wireline “local” and “long distance” consumers. Parsing consumers into technological groups as if they were not the same consumers makes no sense when evaluating the consumer impact of a proposed change. In her analysis, Ms. Behrend examined TNS data to determine the average number of wireline *and* wireless connections purchased by each household and income group, and found that the CoSUS proposal would reduce total USF recovery fees on average.<sup>166</sup> Nextel concedes as much when it complains that although consumers may be better off on average, some will be worse off.<sup>167</sup> Although it is undoubtedly true that some consumers will be worse off, just as some consumers will be better off, neither Nextel nor any other commenter offers any reason why these customer specific impacts should be of public policy concern when, in aggregate, consumers are better off.

Western Wireless argues that a \$1.00 per connection USF assessment could have a deleterious impact on Lifeline subscribers, particularly those receiving service on tribal lands where the service charge is only \$1.00 per month.<sup>168</sup> We agree. For that reason, the CoSUS proposal would not assess USF contributions against any Lifeline connections, and it would

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<sup>164</sup> See Behrend Declaration at ¶ 4(a).

<sup>165</sup> Verizon Wireless *FNPRM* Comments at 4; *see also* VoiceStream *FNPRM* Comments at 2.

<sup>166</sup> See Behrend Declaration at ¶¶ 4(a), 8.

<sup>167</sup> Nextel *FNPRM* Comments at 14.

<sup>168</sup> Western Wireless *FNPRM* at 4.

preclude recovering contributions from those connections. If Western Wireless' concern is that it has not been given eligible telecommunications carrier ("ETC") status in some states and therefore does not qualify to offer Lifeline service, that is an issue it must pursue in separate state or federal proceedings. Western Wireless' objection is not a reason to avoid necessary reform of the current USF assessment mechanism.

There is also no evidence that the switch to a connection- and capacity-based assessment mechanism will cause "rate shock" for residential or wireless consumers, as Sprint suggests.<sup>169</sup> In the first instance, these same consumers that are seeing increased USF charges on their wireless bill will most likely be seeing reduced USF charges on other bills. In addition, there is no evidence that Subscriber Line Charge increases of \$0.85 per month in 2000, and another \$1.00 per month in 2001 caused any "rate shock" for residential consumers. Certainly it did not spark a wave of service disconnections, as residential telephone subscribership has reached its highest-ever levels even with higher SLC charges. With respect to mobile service, VoiceStream concedes, "A 54-cent tax increase, by itself, may not influence a consumer's decision to purchase mobile service."<sup>170</sup> Even the paging carriers submit no economic evidence that the minimal nominal increases in their assessments will cause service migration or disconnections.<sup>171</sup> Concerns about rate shock are unfounded and baseless.

#### **B. The CoSUS Proposal Will Not Harm Small Businesses as a Whole.**

Assertions by commenters that the CoSUS proposal will harm small businesses are unfounded. Verizon's estimate that the Tier 1 multiline business assessment will be \$8.30 per

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<sup>169</sup> Sprint *FNPRM* Comments at 14.

<sup>170</sup> VoiceStream *FNPRM* Comments at 3.

<sup>171</sup> Verizon Wireless *FNPRM* Comments at 7.

Tier 1 connection per month is triple CoSUS' estimate of approximately \$2.75 per connection per month at initial implementation.<sup>172</sup> Verizon's estimate does not add up. At \$8.30 per switched multiline business line per month, using Verizon's own estimate of 66 million business lines in 2002, switched multiline business lines would be contributing nearly \$6.6 billion to universal service, without any contributions from any other connections.<sup>173</sup> This estimated contribution exceeds Verizon's forecast of the size of the USF fund of \$6.2 billion for 2002.<sup>174</sup>

Using the Coalition's estimate of \$2.75 for the initial switched multiline business rate, the Centrex rate would be approximately 30 cents, rather than the 92 cents Verizon asserts.<sup>175</sup> Assuming that this is approximately the same level for the Tier 1 charge once the transitional period is completed, for an interstate DS-1 special access circuit, this would be a Tier 2 charge of \$13.75 per month, as compared to the \$35 per month that Verizon states is typical today.<sup>176</sup> Consistent with concerns raised by ASCENT, the CoSUS proposal also would assess the connection charge based on the customer's service request, rather than the network facilities used by the carrier to provision a service.<sup>177</sup>

Some CLECs have argued that many small business customers would pay more under a per-connection mechanism because these customers have very low interstate usage despite

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<sup>172</sup> Compare Verizon *FNPRM* Comments at 15-16 (estimating a Tier 1 charge of \$8.30 per connection per month) with CoSUS *FNPRM* Comments at 13 n.30 (estimating an initial switched multiline business assessment of \$2.75 per connection per month).

<sup>173</sup> Verizon October 26, 2001 *Ex Parte* at 7 (estimating 66 million business lines in 2002).

<sup>174</sup> *Id.* at 4.

<sup>175</sup> See Verizon *FNPRM* Comments at 16.

<sup>176</sup> *Id.*

<sup>177</sup> ASCENT *FNPRM* Comments at 7.

having several lines. It is of course true that some small business customers could pay more under the Coalition proposal, but some would pay substantially less.

The Coalition reviewed two small-business scenarios that the Commission had included in the press package accompanying its 1997 *Universal Service First Report and Order*.<sup>178</sup>

Scenario One involved a travel agency in Sioux Falls, South Dakota, with three telephone lines for two agents. Each agent makes about 2.5 hours of long distance calls per day. The agency's total long distance bill (for all three lines) is about \$790 per month, and about \$930 including local service. Assuming an interstate/intrastate long distance ratio of 65:35, an IXC revenue-based USF recovery charge of 9.9 percent, and an ILEC connection-based USF recovery charge under the CoSUS proposal of \$3 per multiline business connection, this travel agency's monthly USF recovery charges would decrease from \$52.36 (\$50.83 on the long distance bill and \$1.53 on the local bill) to \$9.00, a savings of \$43.36.<sup>179</sup>

The FCC's second scenario involved a funeral parlor in Anywhere, USA, with three telephone lines used mainly for incoming calls. The owner only makes 15 minutes of long distance calls per month. The funeral parlor's total monthly bill is about \$7 for long distance and \$150 for local service. Under the CoSUS proposal, the funeral parlor's USF payments would increase from \$2.22 to \$9, an increase of \$6.78 per month. This is smaller than the SLC increase that many business customers of price cap LECs experienced in July 1997, and business customers of non-price cap LECs experienced in January 2002, with no evidence of "rate shock."

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<sup>178</sup> Report No. CC 97-24, "Commission Implements Telecom Act's Universal Service Provisions" (rel. May 7, 1997); *see also Universal Service First Report & Order*, Separate Statement of Chairman Reed E. Hundt, 12 FCC Rcd at 8267-80.

<sup>179</sup> *See* n.119, *supra*.

**C. The CoSUS Proposal Protects Multiline Business Users Against Dramatic USF Funding Increases.**

CoSUS agrees with Verizon that permanently calculating the multiline business line assessments on a residual basis would subject business users to too much risk of volatility, particularly as the USF fund is likely to continue to increase over the next five years.<sup>180</sup> The solution, however, is not to jettison a per-connection assessment mechanism, but rather to spread the risk of USF increases and the benefits of USF decreases across all connections. This provides the stability that Verizon contends is necessary, and maintains full public accountability for fund increases.

The CoSUS mechanisms for safeguarding multiline business users against exorbitant USF fees is simpler and more reliable than the periodic reviews proposed by ITAA. Rather than creating a system of annual reviews,<sup>181</sup> the CoSUS proposal simply builds the adjustment into the calculation of the assessment rates. Because each assessment rate goes up or down proportionately in response to changes in the size of the fund relative to changes in the number

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<sup>180</sup> Verizon *FNPRM* Comments at 16-17.

<sup>181</sup> ITAA *FNPRM* Comments at 10-12.

and mix of connections, the risk of fee growth and the benefit of fee reduction is spread across all customer groups.

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